

[COMMITTEE PRINT]

THE RETIREMENT EQUITY TECHNICAL
CORRECTIONS ACT OF 1986
(H.R. 2110)

A COMPILATION OF COMMENTS SUBMITTED
BY THE PUBLIC ON H.R. 2110

TO THE
SUBCOMMITTEE ON
LABOR-MANAGEMENT RELATIONS
OF THE
COMMITTEE ON EDUCATION AND LABOR
HOUSE OF REPRESENTATIVES



APRIL 1986

Serial No. 99-P

Printed for the use of the
House Committee on Education and Labor

U.S. GOVERNMENT PRINTING OFFICE
WASHINGTON : 1986

59-603 O

For sale by the Superintendent of Documents, Congressional Sales Office
U.S. Government Printing Office, Washington, DC 20402

H342-10

COMMITTEE ON EDUCATION AND LABOR

AUGUSTUS F. HAWKINS, California, *Chairman*

WILLIAM D. FORD, Michigan
JOSEPH M. GAYDOS, Pennsylvania
WILLIAM (BILL) CLAY, Missouri
MARIO BIAGGI, New York
AUSTIN J. MURPHY, Pennsylvania
DALE E. KILDEE, Michigan
PAT WILLIAMS, Montana
MATTHEW G. MARTINEZ, California
MAJOR R. OWENS, New York
RICK BOUCHER, Virginia
CHARLES A. HAYES, Illinois
CARL C. PERKINS, Kentucky
TERRY L. BRUCE, Illinois
STEPHEN J. SOLARZ, New York
MERVYN M. DYMALLY, California
DENNIS E. ECKART, Ohio
TIMOTHY J. PENNY, Minnesota
CHESTER G. ATKINS, Massachusetts

JAMES M. JEFFORDS, Vermont
WILLIAM F. GOODLING, Pennsylvania
E. THOMAS COLEMAN, Missouri
THOMAS E. PETRI, Wisconsin
MARGE ROUKEMA, New Jersey
STEVE GUNDERSON, Wisconsin
STEVE BARTLETT, Texas
ROD CHANDLER, Washington
THOMAS J. TAUKE, Iowa
JOHN K. MCKERNAN, Jr., Maine
RICHARD K. ARMEY, Texas
HARRIS W. FAWELL, Illinois
PAUL B. HENRY, Michigan

SUBCOMMITTEE ON LABOR-MANAGEMENT RELATIONS

WILLIAM (BILL) CLAY, Missouri, *Chairman*

WILLIAM D. FORD, Michigan
DALE E. KILDEE, Michigan
MARIO BIAGGI, New York
CHARLES A. HAYES, Illinois
MERVYN M. DYMALLY, California
CHESTER G. ATKINS, Massachusetts
MAJOR R. OWENS, New York
AUGUSTUS F. HAWKINS, California
(Ex Officio)

MARGE ROUKEMA, New Jersey
ROD CHANDLER, Washington
RICHARD K. ARMEY, Texas
STEVE BARTLETT, Texas
HARRIS W. FAWELL, Illinois
JAMES M. JEFFORDS, Vermont
(Ex Officio)

FOREWORD

The Retirement Equity Act of 1984 (REA), P.L. 98-397, was enacted on August 23, 1984. It amended both the Employee Retirement Income Security Act of 1974 (ERISA) and the Internal Revenue Code of 1954 to improve the delivery of retirement benefits and provide for greater equity under private pension plans for workers, their spouses, and their dependents. It accomplished those goals primarily through three types of changes: (1) revision of minimum participation, vesting, and benefit accrual standards, (2) expansion of the survivor benefit requirements, and (3) clarification of the responsibility of plan administrators to honor qualified domestic relations orders issued under State law.

Since the enactment of REA, the Subcommittee has become aware of certain problems with respect to the operation of some of the provisions of the Act. On April 18, 1985, H.R. 2110, a bill to make technical corrections to REA, was introduced. I joined with the Chairman of the Committee on Ways and Means, Mr. Rostenkowski, its Ranking Republican, Mr. Duncan, and the Ranking Republican on the Subcommittee on Labor-Management Relations, Mrs. Roukema, in introducing the bill.

Because of the technical nature of the issues addressed in H.R. 2110, the Subcommittee requested written comments on the bill. This committee print is an unedited compilation of the comments we received.

Hon. WILLIAM L. CLAY,
Chairman.

LIST OF COMMENTS (BY ORGANIZATION)

	Page
American Academy of Actuaries	2
American Council of Life Insurance	10
American Society of Association Executives	40
American Society of Pension Actuaries.....	47
American Telephone & Telegraph (AT&T).....	54
Association of Private Pension and Welfare Plans	59
Buck Consultants	71
Chevron Corporation	74
ERISA Industry Committee	95
Gibson, Dunn & Crutcher.....	106
Investment Company Institute.....	109
National Coordinating Committee for Multiemployer Plans	119
National Rural Electric Cooperative Association	154
North Carolina Commission of Labor	157
Older Women's League	249
Small Business Council of America.....	251
Snell & Wilmer.....	278
Williams & Connolly	282

MAJORITY MEMBERS
WILLIAM BRAD CLAY, MISSOURI, CHAIRMAN
WILLIAM T. ROYCE, MISSOURI
DALE E. KILDEE, MISSOURI
BENNO RANKIN, NEW YORK
CHARLES A. HAYES, ALABAMA
BENNY W. STEINLEY, CALIFORNIA
CHESTER G. ATHERS, MASSACHUSETTS
MAJOR E. OWENS, NEW YORK
AUGUSTUS F. HARRIS, CALIFORNIA
EX OFFICIO

(PH) 225-6146 (DS) 229-6495



COMMITTEE ON EDUCATION AND LABOR

U.S. HOUSE OF REPRESENTATIVES

2451 RAYBURN HOUSE OFFICE BUILDING
WASHINGTON, DC 20515

SUBCOMMITTEE ON
LABOR-MANAGEMENT RELATIONS

MINORITY MEMBERS
CARLE SCHULZ, NEW JERSEY
BOB CHANDLER, WASHINGTON
RICHARD E. ARMSTRONG, TEXAS
STEVE BARTLETT, TEXAS
HARRY W. FARRER, ALABAMA
JAMES M. JEFFORDS, VERMONT
EX OFFICIO

May 16, 1985

NOTICE OF DEADLINE FOR COMMENTS ON H.R. 2110

William L. Clay, Chairman of the Subcommittee on Labor-Management Relations, today announced that in lieu of scheduling a hearing on H.R. 2110, a bill making technical changes to the Retirement Equity Act of 1984 (P.L. 98-397), the Subcommittee will accept written comments on the bill. The Subcommittee intends to publish a compilation of the comments submitted.

Anyone wishing to submit comments for the record should send five copies of the statement to the Subcommittee at the address above, to the attention of Phyllis Borzi, Pension Counsel.

The deadline for submission is June 7, 1985.

(1)

AMERICAN ACADEMY OF ACTUARIES

STEPHEN G. KELLISON, M.A.A.A. Executive Director

May 29, 1985

The Honorable William L. Clay, Chairman
Subcommittee on Labor-Management Relations
Committee on Education and Labor
United States House of Representatives
2451 Rayburn House Office Building
Washington, D.C. 20510

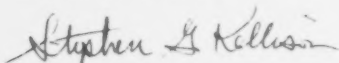
Re: H.R. 1800, Technical Corrections Act of 1985

Dear Mr. Clay:

Enclosed is a statement on behalf of the American Academy of Actuaries concerning the Technical Corrections Act of 1985 (H.R. 1800). It is our understanding that your subcommittee will not be holding hearings on this bill. Given the fact, however, that hearings on the bill have been held by the Committee on Ways and Means on May 16, we thought that our comments for the record of that hearing would be of interest to you and to your subcommittee.

The comments were prepared by the Academy's subcommittee on Health and Welfare Plans. They would be happy to answer any questions about this statement or to provide further information on request. We appreciate this opportunity to submit this statement for your consideration.

Respectfully submitted,



Stephen G. Kellison
Executive Director

AMERICAN ACADEMY OF ACTUARIES

STATEMENT TO
THE HOUSE COMMITTEE ON WAYS AND MEANS
AND TO
THE SUBCOMMITTEE ON LABOR-MANAGEMENT RELATIONS
OF THE HOUSE COMMITTEE ON EDUCATION AND LABOR

ON BEHALF OF THE
SUBCOMMITTEE ON HEALTH AND WELFARE PLANS
OF THE AMERICAN ACADEMY OF ACTUARIES
HEARINGS ON THE TECHNICAL CORRECTIONS ACT OF 1985

MAY 29, 1985

On May 16, 1985, the House Committee on Ways and Means held hearings on the Technical Corrections Act of 1985. The comments below are submitted for the record of those hearings and to the Subcommittee on Labor-Management Relations of the House Committee on Education and Labor.

PURPOSE

The American Academy of Actuaries ("Academy") appreciates the opportunity to submit comments on the Technical Corrections Act of 1985. This document contains comments on issues relating to premium stabilization reserves, setting actuarial assumptions, disability income benefits, and the definition of a qualified actuary.

BACKGROUND

The Academy is a professional association of over 7,600 actuaries involved in all areas of specialization within the actuarial profession. Included within our membership are approximately 85% of the enrolled actuaries certified under the Employee Retirement Income Security Act of 1974 (ERISA), as well as comparable percentages of actuaries specializing in actuarial services for other employee coverages such as life, health and disability programs. As a national organization of actuaries, the Academy is unique in

that its membership consists of actuaries with expertise in all areas of actuarial specialization.

The Academy does not advocate major public policy positions, in such areas as tax legislation, which are not actuarial in nature. The Academy views its role in the government relations arena as providing information and actuarial analysis to public policy decision-makers, so that policy decisions can be made with informed judgment. It is our belief that the training and experience of Academy members allow a unique understanding of current practices in employee benefits. Our intention is to communicate that understanding in ways that assist policy decision-makers.

COMMENTS

Premium Stabilization Reserves

The description of the Technical Corrections Act of 1985 states that certain amounts held by an insurance company for a reasonable premium stabilization reserve may not be treated as a fund for purposes of Section 419.

A premium stabilization reserve, in order to be considered reasonable, should reflect the nature of the coverages to which it applies. A coverage that is characterized by frequent, relatively small claims requires a smaller reserve than a coverage characterized by large, infrequent claims. Furthermore, a larger reserve should be considered reasonable on coverages where fewer lives are exposed. Claim costs can fluctuate significantly from year to year, and a reasonable premium stabilization reserve can provide protection against fluctuation.

The level of reserves which might be considered reasonable also depends on the nature of the group insured. Where a premium is collected directly from individuals covered, it is desirable to maintain those premiums at a stable level from year to year. If premiums increase significantly, covered lives who are generally better risks will drop out of the group. The remaining lives will require further premium increases, and the plan will continue to decline in size. Thus, a stabilization reserve for this sort of group should be significantly higher than for a conventional employer plan in order to prevent a declining enrollment spiral.

Examples of groups where higher levels of reserves are reasonable are employee-pay-all plans, associations of individuals, and to a lesser extent, associations of employers and other multiple employer plans.

The appropriate level of reserves on a particular group can be determined based on type and design of benefit provisions, and the nature of the group covered. This level of reserve can vary from group to group.

Actuarial Assumptions

As in any actuarial assignment, the setting of appropriate assumptions is a key ingredient in establishing funding levels. The provisions relating to welfare benefit plans funded through VEBAs in the Deficit Reduction Act of 1984 require that assumptions be reasonable in the aggregate. This is quite appropriate and follows the precedent set by ERISA in the pension area. However, the Conference Report goes further and indicates that "in addition to requiring that actuarial assumptions are to be reasonable in the aggregate, Treasury regulations may prescribe specific interest rate and mortality assumptions to be used in all actuarial calculations." Such a simplistic approach would

ignore the fact that experience is different from plan to plan for a variety of reasons (age/sex composition, benefit utilization tendencies of group, nature of work, geographical area, etc.). Attempting to mandate any set of uniform assumptions will inevitably result in inappropriate assumptions being used for large numbers of plans. Setting appropriate actuarial assumptions requires the application of actuarial judgment to fit the facts and circumstances at hand.

We are concerned at the prospect that specific actuarial assumptions might be prescribed for funded welfare benefit plans. We believe the approach used in ERISA for setting actuarial assumptions for pension valuations is much more appropriate. The treatment of future increases in claim costs on post-retirement benefits is of particular concern. Under the Deficit Reduction Act of 1984, increases in claim costs due to any source such as inflation, changes in utilization patterns, etc. could only be funded each year after the increase has occurred, rather than through advance funding. The net effect is that these limits in general will be substantially below the full, level cost of the benefits promised. This provision effectively discourages employers who wish to adequately fund retiree welfare benefits as they do pension plans.

Definition of Disability

The Conference Committee has expressed its intent that with regard to welfare benefit funds established for providing disability benefits that a disability be defined as "any serious physical or mental impairment which causes an inability to perform a substantial portion of the duties of an individual's ordinary employment." The Committee further expressed their intent that funding of claims with respect to an indefinite period of time be allowed only in connection with disabilities that are determined to be long term disabilities. Such disabilities are "those which (1) a medical evaluation determines is

expected to last more than 12 months and (2) has persisted for at least five months."

The Conference Committee's definition of disability has two serious defects. First, it does not recognize disabilities that are not expected to last twelve months under a long term disability plan. Many serious disabilities will persist beyond five months, but will terminate either by death or recovery within one year of the onset of disability. Second, the definition requires that the claim persist for at least five months and many long term disability plans employ a shorter elimination period.

There are several definitions of disability which are commonly used in conjunction with disability income plans. The definition which is incorporated into a particular plan document will reflect the plan sponsor's employee benefit philosophies and policies, as well as the level of costs it is willing to incur.

A plan sponsor is not likely to modify the definition of disability within its plan document to conform with the Conference Committee's definition. As a result, one definition of disability would be used for benefit determination and a second would be employed for the purposes of determining qualified funding limits. This qualification of certain disabilities for the purpose of determining funding limits could result in an unrelated business income tax to the fund if it is funded to meet its future obligations according to reasonable actuarial assumptions as to morbidity, mortality and interest. On the other hand, if fund accruals are limited to be in accord with the Conference Committee's definition of disability, the fund may be insufficient to meet its future obligations.

We recommend that a disability income plan funding level be determined using actuarial techniques and reasonable assumptions as to morbidity, mortality and interest reflecting the definition of disability incorporated into the plan document.

Short Term Versus Long Term Disability Plans

The Conference Committee limits funding for short term disability plans to five months of benefit payments. Short term disability plans most commonly provide for three, six or twelve months of payment. We recommend that a short term disability plan funding limitations be defined in a manner consistent with the plan maximums.

Definition of Qualified Actuary

Actuarial analysis of employee welfare benefit plans demands the expertise of specialists in welfare plans, employing actuarially sound methods which reflect characteristics unique to those particular welfare plans. Included are characteristics such as the analysis of past health care utilization, adjustments to reflect the changes of plan design or demographics, assessments of claim liabilities, analysis of claim trends (including inflation and utilization patterns) and projections of financial experience. Only actuaries specializing in these programs are properly qualified to so examine employer welfare benefit plans. For example, an enrolled actuary under ERISA has satisfied qualification standards for practice in the pension area, but such an individual may or may not be qualified when it comes to employee health and welfare plans. We strongly urge that direct participation of the actuarial profession be utilized in defining necessary qualifications for actuarial services to these plans. The Academy has a strong commitment to professional standards and self-regulation. We are prepared to work closely with the government if regulations regarding actuarial qualifications are to be developed.

SUMMARY

The actuarial profession, as represented by the American Academy of Actuaries, appreciates the opportunity to present our testimony and wishes to offer any possible assistance to the governmental bodies involved with employee welfare benefit plans. Because we understand past and present practices in this area, we believe that we can assist in identifying and weighing the merits of employee benefit plan alternatives for the future. We hope the comments presented in this statement will be useful in helping Congress deal appropriately with the complex area of employee benefits.

AMERICAN ACADEMY OF ACTUARIES

Committee on Health

E. Paul Barnhart, Chairman

Subcommittee on Health and Welfare
Plans

Thomas G. Nelson, Chairman

Alan D. Ford
Anthony J. Houghton
Martin J. Loughlin
William J. Miner
Richard Ostuw
Jeffrey P. Petertil
Thomas G. Ruehle

American Council of Life Insurance

1850 K Street, N.W.,
Washington, D.C. 20006
(202) 862-4335

Phyllis H. Gerstell
Senior Counsel

June 5, 1985

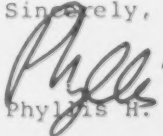
Ms. Phyllis Borzi
Pension Counsel
Subcommittee on Labor and
Management Relations
Committee on Education and Labor
2451 Rayburn House Office Building
Washington, D. C. 20515

Dear Ms. Borzi:

Enclosed for inclusion in the hearing record,
are the ACLI's comments on H.R. 2110, the Retirement
Equity Act technical corrections bill.

Please let me know if you would like any
additional information.

Sincerely,



Phyllis H. Gerstell

Enclosures
/ha

STATEMENT OF THE
AMERICAN COUNCIL OF LIFE INSURANCE

on

H. R. 2110, Making Technical Corrections
to the Retirement Equity Act of 1984

Before the Subcommittee on Labor Management Relations
of the Committee on Education and Labor
of the United States House of Representatives

June 5, 1985

MR. CHAIRMAN AND MEMBERS OF THE SUBCOMMITTEE:

The following comments on H.R. 2110, making technical corrections to the Retirement Equity Act of 1984, are offered on behalf of the American Council of Life Insurance ("ACLI"). The ACLI is a trade association representing 615 life insurance companies. Together, these companies hold 95 percent of the life insurance written in the United States and 97 percent of the assets of insured pension plans.

COMMENTS ON H.R. 2110, THE RETIREMENT EQUITY ACT
TECHNICAL CORRECTIONS ACTA. Effect of The Retirement Equity Act ("REA") on Single
Premium Annuity Contracts

While the ACLI applauds efforts to correct technical problems under REA, we are disturbed that H.R. 2110, the Retirement Equity Act Technical Corrections Act, leaves unaddressed very significant issues regarding terminated plans that were so superficially treated in REA. We think it fair to say that throughout Congressional consideration of REA, there was no contemplation that all of the procedural requirements of that legislation would be extended past plan termination. While we support the basic protections provided plan participants by REA, it has become clear to us since enactment that, when considered in the context of the group annuity arrangements purchased by plan sponsors as part of the process of winding up the affairs of the plan, certain REA provisions impose unnecessary expense and uncertainty on employers and insurers.

Typically, when a plan sponsor of a terminated defined benefit plan winds up the affairs of that plan, it purchases a single premium non-participating group annuity contract ("SPAC"), under which the entire benefit rights of each plan participant are fully guaranteed through an irrevocable commitment issued to the plan participants by a private insurer. Prior to enactment

of REA, participants who elected a lump sum payment of their benefits were permitted, under the regulations of the Pension Benefit Guaranty Corporation ("PBGC"), the agency charged with the enforcement of ERISA's plan termination provisions, to irrevocably elect this benefit option and receive an immediate distribution in lieu of the insurer's commitment to provide an annuity at retirement age. This procedure predated purchase of the annuity arrangement and was effectuated by the plan sponsor--not the insurer. In lieu of a cash payment, a participant could elect to be covered by the annuity contract (choosing any of a variety of annuity options) generally determined as of the annuity commencement date and calculated using the insurance company's interest rates and actuarial factors, as specified in the contract negotiated at plan termination between the insurer and the sponsor of the terminating plan. Once a participant elected to receive a commitment to an annuity, if any, insurers permitted a later election of a lump sum payment.

We recognize that certain of the new requirements imposed by REA necessitate appropriate adjustments in the rules governing plan terminations. So, for example, participant elections in favor of a single life annuity or a lump sum should require spousal consent, even if a plan is terminating. Similarly, elections with respect to benefit options that are made by the participant at the time the plan terminates appropriately should be converted using the interest rates and factors specified in

the plan prior to plan termination, as required by Code Section 401(a)(25) and Revenue Ruling 79-90.

Beyond these requirements, however, are a variety of REA imposed procedural requirements which ignore the distinctions between a terminated plan and an ongoing plan. Mandated application of these requirements as the exclusive method of complying with the survivor benefit and anti-cut-back provisions of REA violates the long-held premise of our private pension system that plan establishment and termination are voluntary and that, after plan termination, a participant's rights under an ongoing plan are settled.

While it may be appropriate to protect past accruals in an ongoing plan after a plan amendment, participants in a terminated plan have no expectation of future service or benefit accrual after the date of termination. Accordingly, the ACLI believes there is a clear qualitative distinction between an amendment to an ongoing plan and the termination of a plan. After plan termination, rights which attach to an individual's status as a plan participant are no longer protected. Just as participants are no longer credited with additional vesting and no longer entitled to periodic reports with respect to their benefit rights, summary plan descriptions and the like, it is fundamentally inconsistent with the notion of terminated plans to permit unlimited revocability of benefit elections, additional benefit

entitlement based on events occurring after the date of plan termination, and the continuing imposition of the notice and recordkeeping obligations of an ongoing plan sponsor on the insurer.

In the context of plan termination, the insurer is no more than a vendor of a product required under the law to effectuate a plan termination under Title IV of ERISA. The insurer's product is fully regulated under state law, and its obligations to former plan participants derive from the contractual relationships between the individual annuitant and the insurer, rather than from the provisions of the now terminated plan. An employer who decides to establish and maintain an ERISA-covered and tax qualified plan thereby obligates itself to conform to the rules imposed by those statutes. The issuance of a SPAC in satisfaction of a plan's liabilities under Title IV should extinguish the plan administrator's obligations and not, as has been suggested by some since REA, merely transfer his obligations to the insurer of the annuity guarantee. This position is clearly embodied in the Department of Labor's regulations under ERISA defining "employee benefit plan" (29 CFR 2510.3-3) and also in the PBGC regulations defining "participant" for purposes of premium payments (29 CFR 2610.2).

Our detailed comments on specific issues relating to SPAC's

where further technical corrections to REA are needed follow below.

1. Treatment of Optional Forms of Benefits. Section 301 of REA amended Section 411(a)(6) of the Code and Section 204(g) of ERISA to provide that a plan amendment which, with respect to benefits attributable to service before the amendment has the effect of eliminating an optional form of benefit, shall be treated as an amendment reducing accrued benefits. The anti-cut-back rules of REA Section 301 further provide that a participant's accrued benefit is only considered to be reduced if the removal of the optional form of benefit results in the participant's loss of a "valuable right". The Secretary of the Treasury is given authority to issue regulations relating to conditions under which the removal of an optional form of benefit will and will not be regarded as the removal of a valuable right.

Under the new statutory rules, optional forms of benefits are treated, for purposes of the anti-cut-back requirements, in some fashion as a participant's accrued benefit. Furthermore, it is possible that regulations ultimately issued will interpret the assumptions, interest rates and conversion factors used by a plan to calculate the amount of a participant's benefit under any particular optional form of benefit as forming part of a participant's accrued benefit which may not be reduced by a plan amendment. Such a position, particularly in the small plan area,

would create serious problems for insurers who issue SPAC's to fund a terminated plan. More importantly, this position would, in many instances, increase the costs of terminating plans and ultimately decrease benefits for participants and beneficiaries.

As it is highly likely that an insurer's current internal interest rate assumption for lump sum distributions will be considerably higher than that used by the plan or PBGC, the opportunity is created for adverse selection against the insurer by the participant. Since little or no protection for such adverse selection currently exists, an insurer would be forced to charge a higher price to protect against this risk. Similar results arise in the case of subsidized optional forms of payment where the extent of utilization of the option cannot be reasonably predicted at the time of plan termination.

To resolve this problem, the ACLI suggests that a technical correction to REA be enacted to provide that, upon plan termination, only the participant's initial choice of benefit need be governed by the anti-cut-back in accrued benefit rules. Under this approach, a participant would be given a one-time right to select any optional form of benefit using the plan's assumptions, conversion factors, interest rates and procedures for determining actuarial equivalence. After having made this one-time election, a participant could later choose a different form of payment

(limited to those previously available under that plan which provide "valuable rights").

Under the ACLI proposed rule, the insurer would provide the participant with the same alternatives as if the plan had continued. The only exception would be that, for subsequent changes after the initial election by the participant, the insurer's (rather than the plan's) interest rates, conversion factors and procedures for determining actuarial equivalence for optional forms of benefits could be used. This change would allow appropriate distinctions between ongoing and terminated plans and would allow plan amendments in an ongoing plan to be properly subject to the anti-cut-back rules, without encompassing amendments to terminated plans in a way that would make termination more expensive and complicated.

2. Qualified Pre-Retirement Survivor Annuities and Qualified Joint and Survivor Annuities. Another area of substantial concern in our industry relates to the interaction of two prominent sections of REA concerning Qualified Pre-Retirement Survivor Annuities ("QPSA's").

Section 203 of REA provides for the furnishing of a QPSA -- an annuity to a surviving spouse equivalent to 50% of the participant's accrued benefit. At the same time, REA Section 301 prohibits a cut-back in accrued benefits, and treats certain

cut-backs in early retirement benefits, retirement-type subsidies and optional benefit forms, as cut-backs in accrued benefits.

Prior to the passage of REA, it seemed clear that a pre-retirement death benefit was not part of the accrued benefit nor was it treated as such. This position was embodied in the Internal Revenue Code Section 411 regulations, which excepted death benefits from the definition of "accrued benefits" (Treasury Regulation Section 1.411(a)-7(a)(1)).

Section 301 of REA does not mention survivor benefits as a type of benefit to be treated as an accrued benefit. On the contrary, the legislative history expressly states that death benefits are not to be considered as a "retirement-type subsidy" under Section 301 such that the anti-cut-back provision would be applicable (See Cong. Rec. of Aug. 2, 1984 - S9679 and S9680.)

In light of this fact, the ACLI believes the QPSA to be outside the scope of the anti-cut-back rules. However, in the event this position is not adopted, we believe the survival of the QPSA is only workable if there is a clear definition of who is the "surviving spouse" in the case of a terminated plan for purposes of REA survivor benefits and the spousal consents necessary to the waiver of any such benefits.

The treatment of this problem by the Technical Corrections Act (H.R. 2110) in an analogous area--that of plan loans--is

instructive. In the plan loan area, where the pledging of an accrued benefit as collateral may well have an impact in the future--and a negative impact on a different spouse--H.R. 2110 recognizes that spousal consent to the pledge at the time of the loan will control the impact in the future even if there is a different spouse at that time.

The ACLI suggests that those considerations which are inherent in the above noted loan provision proposal may well be even more pertinent in the area of plan termination. We also suggest that the protection of the individual who is the spouse as of plan termination--despite subsequent occurrences--is not inconsistent with, and may be in furtherance of, the policies underlying REA. It is, after all, the "termination date" spouse who has shared in the marital partnership with the plan participant during the years of benefit accrual.

With regard to plan termination, spousal consent is a particularly troublesome problem by virtue of Internal Revenue Code Section 417, as added by Section 203 of REA, which states that a plan must provide a Qualified Joint and Survivor Annuity ("QJ&S") to a married participant unless such participant waives that benefit with the consent of his or her spouse.

In the case of the QPSA, the election period which would require spousal consent extends to the participant's death. In the case of the QJ&S, that election period (together with the

necessity of spousal consent) begins 90 days prior to and ends with the annuity starting date (the date as of which the payments under the plan commence).

Internal Revenue Code Section 417 (a)(2)(B) states that "... Any consent of a spouse (or establishment that the consent of a spouse may not be obtained) under the preceding sentence shall be effective only with respect to such spouse."

In the context of an ongoing plan where the relationship among the respective participants, plan sponsor and plan administrator is normally subject to adjustments (particularly in the area of marital status) there is perhaps less concern regarding these matters.

The difficulty arises, however, when the plan has terminated and (perhaps) the plan sponsor is no longer in existence. The plan has sought a guarantee of its obligations through purchase of annuity contracts or certificates but to a large extent the guarantee is imposed upon what may be a fluid situation.

Thus, a variety of questions arise in the area of plan termination, survivor benefits and spousal consents concerning the timing of events, for example:

o If the plan has terminated and the participant is single at the time, would a subsequent marriage necessitate a spousal consent to the form of benefit chosen? In the absence of such

consent, would the benefit need to be converted into a QJ&S? What if the benefit has been distributed and has been partially or fully utilized?

o If the participant, single at plan termination but subsequently married, dies prior to the annuity starting date, would a QPSA have to be provided for the spouse?

o Again, in the context of a terminated plan, assume a participant is married and a QJ&S is provided for, would subsequent divorce negate that survivor benefit?

o If that participant remarries, which spouse is entitled to the survivor benefits?

o If the prior spouse had consented to an alternate form of benefit, does that consent have any impact on the subsequent spouse?

The law would seem to say that in all these circumstances events subsequent to the plan termination may still have to be accounted for. The ACLI believes, however, that such a rule places the insurer in an untenable situation.

The purpose of a plan buying annuities is to provide guarantees and certainty with respect to its obligations accrued to the date of the plan's termination. We suggest that it would be in furtherance of that policy which requires such guarantees and in

furtherance of the underlying policies of REA if, for purposes of IRC Section 417, the surviving spouse is defined as the spouse as of the date of plan termination for purposes of the provisions relating to survivor benefits and the notices and consents pursuant to those benefits.

3. Notice Requirements As amended by REA, ERISA Section 205(c) and IRC Section 417(a) (3) require plans to provide participants with written notice of the requirements of a QJ&S and the rights and elections associated therewith, including the requirement that a spouse's consent is needed to waive the joint and survivor benefit. This notice must be provided within a reasonable period of time before the annuity starting date. Similarly, an explanation of the QPSA must be provided to each participant sometime during the period when the participant is between ages 32 and 35.

ERISA Section 205(c) (6) and IRC Section 417(a) (5) provide that, for separated participants, the applicable election period for the QPSA cannot begin later than separation from service. Although the notice requirement contained in ERISA Section 205(c) (3) (B) and IRC Section 417(a) (3) (B) does not explicitly explain when notice should be given for terminated employees, because notice should precede the election period it would appear that in such cases notice would be given between ages 32 and 35, but not later than separation from service.

These provisions cause serious administrative problems for insurers issuing SPAC's to terminated plans. After plans have been terminated it is very difficult for an insurer to properly give notice to covered employees. In the case of an ongoing plan, the nexus of employment enables the plan administrator to keep accurate and current records of the marital status, age and work status of covered employees. An insurer, by contrast, is not in a position to do so. The problem is severe where the termination is accompanied by the employer's closing of operations. In such a situation the insurer has no one to turn to to ascertain the location and the marital status of the participant. The problem is also acute where participants are still employed by the plan sponsor after plan termination. Because the insurer is not in a position to know when an employee severs employment, it can hardly know when to provide notice for the qualified pre-retirement benefit.

The ACLI proposes that in the case of terminated plans notice should be given to employees at the time of plan termination. In our view this would be both an easy and equitable solution to the above-described problem. At the time of plan termination the employee population is well defined. Furthermore, at that time there is always a plan administrator (independent of whether the employer plans to continue operations) from whom the insurer can get the information which it needs to properly provide notice. Significantly, the purpose of REA would

not be compromised under the proposal. At the time of termination, employees are most alert to their rights under a plan and a notice would therefore have its most meaningful impact.

4. IRC Section 411(d)(6), ERISA Title I Section 204(g) and ERISA Title IV. REA prohibits amendments which cause cutbacks in accrued benefits, subsidies, early retirement benefits or optional forms of benefits. Neither the Code nor the parallel ERISA Title I provision deals with termination of a plan.

To avoid the possibility of regulatory duplication and conflict, we propose an amendment to both Code Section 411(d)(6) and ERISA Section 204(g) which would state that nothing therein affects the rules and principles established in ERISA Title IV and PBGC regulations for terminated plans.

As the statutes now read, Title IV continues to be supreme in the plan termination area. Since the enactment of ERISA, Title I and the Code have both prohibited the cutback of accrued benefits. Despite the fact that neither statute provided an exception for terminated plans, accrued benefits have been routinely reduced in terminating plans with assets sufficient to cover guaranteed benefits but insufficient for all benefits. In these cases, assets have been allocated and benefits distributed by guaranteed annuity certificates in accordance with PBGC rules and practice. There is nothing in the statutes themselves after

REA to change this. Only the Senate Finance Committee Report suggests a change (S. Rep. No. 98-575, p. 31 (1984)).

It is our view that the question of the benefits to be provided by a terminated plan should be resolved exclusively under the provisions and principles of Title IV--the only Federal statutory scheme dedicated solely to plan terminations. Title IV deals comprehensively with all the issues surrounding the plan termination event including the priorities in which benefits are to be provided and the conditions to be continued post-termination. Purporting to extend Section 411(d)(6) to provide authority for creating asset allocation and benefit priority rules and post-termination procedures will create confusion, conflict and uncertainty through unnecessary regulatory duplication and in certain cases will result in reduced accrued benefit coverage. A technical correction such as we propose would provide a single clear consistent rule for plan terminations--the rules developed under Title IV of ERISA.

5. Retirement-Type Subsidies. Section 301 of REA amended Code Section 411(d)(6)(B) and Section 204(g) of ERISA to provide that a plan amendment that has the effect of eliminating or reducing an early retirement benefit or a retirement-type subsidy with respect to benefits attributable to service before the amendment is treated as a prohibited reduction in the participant's accrued benefit. In the case of retirement-type sub-

sidies, this prohibition applies only with respect to a participant who satisfies (either before or after the amendment) the pre-amendment conditions for the subsidy. Moreover, Rev. Rul. 85-6 (IRB 1985-5, p.10) provides that in a proposed termination of a defined benefit pension plan, the plan will fail to meet the requirements of Code Section 411(d)(6) as amended unless an early retirement subsidy is provided for participants who satisfy the pre-termination subsidy requirements after the termination of the plan.

In the case of a terminated plan, the insurer who issues a SPAC must make assumptions as to the number of plan participants who have not satisfied the conditions for the subsidy prior to termination of the plan but will eventually qualify for the subsidy after the plan terminates. Since the risk is uncertain the insurer must use a conservative (and costly) assumption to price the SPAC. This makes the price of a SPAC more expensive than if eligibility for the subsidy were more certain at the time of plan termination. Moreover, the insurer is often required to do costly administrative work to determine who becomes eligible for the subsidy and when that occurs. While it is possible that in many cases, such as the one described in Rev. Rul. 85-6, an employee can satisfy the conditions for the subsidy after termination of the plan, it is also true that in many cases the conditions for eligibility for the subsidy can never be satisfied after the plan terminates. For example, a plan may provide that

to be eligible for the subsidy an employee must complete a certain number of years of plan participation (in addition to meeting an age requirement). In such cases, an employee cannot receive credit for additional years of plan participation in any year following the year of plan termination. Similarly, a contributory plan may require a certain number of years of service (in addition to the attainment of a specified age) to be eligible for the subsidy. Under these plans, employees do not get credit for years of service unless they contribute to the plan. Since no contributions are made to a terminated plan, no additional years of service are earned by employees. Finally, under certain conditions employees would not be able to satisfy a service requirement after the termination of a plan if the employer who previously maintained the terminated plan was no longer in existence (due to a sale, spin-off, acquisition, bankruptcy, etc).

To resolve this problem, the ACLI proposes a technical correction to REA to provide that retirement-type subsidies must be provided to employees who have not satisfied the conditions for the subsidy prior to plan termination only if it is possible under the terms of the plan immediately prior to plan termination to satisfy the conditions for the subsidy after the plan terminates.

B. Other Comments

Our section by section comments on areas where we believe H.R. 2110 (the "Act") needs further clarification or correction follow below:

1. Act Section 2(a)(1)(A) - We suggest that the change to paragraph (4) of Section 411(d) be modified by the addition of the words "as an employee" so that it reads "...participant was performing services for the employer as an employee as of the close...." This change would explicitly distinguish employees from independent contractors who are not eligible for benefits or credit under this method.
2. Act Section 2(b)(2)(A&B)(i) - It is our understanding that Code Section 401(a)(11)(B)(iii)(III) will not be triggered by a rollover since, in order for a participant to have received a distribution which he or she can roll over, the joint and survivor requirements would already have had to have been satisfied by the plan making the distribution. In light of this, we believe the reference to "indirect transfers" in Act Section 2(b)(2) should be deleted, since this language would seem to apply only to rollovers. In this way, the provision would only cover a direct trustee-to-trustee transfer.

3. Act Section 2(b)(2)(A&B)(ii) - We suggest that this provision, clarifying transferee plan rules, be modified to read "...if the plan separately accounts for these assets and any income therefrom." In our view, a plan should be able to set up a segregated account for transferred assets only, but not have segregated accounts for other assets and still satisfy the purposes of this paragraph.
4. Act Section 2(b)(4) - Under this section of the Act, a spouse must agree in writing to a loan to the participant if any part of the account balance is pledged as security. Only if such consent is obtained may the plan foreclose on a defaulted loan. The effective date of this provision is April 18, 1985.

Obviously, April 18 has already passed and loans are still being negotiated under the requirements of existing law. Accordingly, we believe the effective date of this provision should be changed to the date of enactment.

In addition, we assume that the requirements for spousal consent under this loan provision are the same as for spousal consent to an election under Code Section 417(a)(2). If this is the case, we suggest that this be explicitly stated in the statute.

5. Act Section 2(c)(4)(A)(v) - While the change to add subparagraph (A) to Code Section 414(p)(9) is necessary, the limitation in subparagraph (B) to the present value of payments to an alternate payee of \$3,500 creates a real problem and should be eliminated.

First, the \$3,500 amount is, in our opinion, too low. Under Code Section 414(p)(4), an order may require a distribution significantly in excess of \$3,500 before a participant has separated from service.

Moreover, using the entire value of the accrued benefit as the appropriate limit is inconsistent with the provisions of Code Section 411(a)(7), which provides that "the plan may disregard service performed by the employee with respect to which he has received (i) a distribution of the present value of his entire nonforfeitable benefit if such distribution was in an amount (not more than \$3,500) permitted under regulations...." If the change in Section 401(a)(11) was not deliberate, a suggested clarification is to insert the word "nonforfeitable" following "If the present value of any". If this change was intended, inserting the words "the nonforfeitable portion of" following "\$3,500," would clarify the provision.

In this regard, we note that a similar ambiguity exists in Code Section 417(e) (1) and (2) (A). To eliminate any question, in both cases the words "nonforfeitable portion of the" should be inserted before the words "present value" the first place it appears.

6. Act Section 2(d) (1) - The change in the rules for the explanation of a distribution eligible for rollover treatment should not be made retroactively effective (as is the case by virtue of Act Section 3). Such retroactive application in our view unfairly creates a compliance requirement which no one could reasonably have foreseen. We suggest instead that this change be made effective as of the date which is no less than six months after the date of enactment.
7. Act Section 2(f) (1) - While this retroactive protection against a double death benefit liability is very welcome, it seems unfortunate that it must be limited to the period before the plan year beginning in 1985. As a practical matter, there are numerous plans relying on old prototype documents or which, for various reasons, will be slow to comply with these new requirements until the first death under the plan occurs. There seems to be no good reason why this provision could not be redrafted to apply on a permanent

basis to any situation where the pre-retirement survivor annuity requirements are in effect. Such a change would not lessen protection for the spouse and it could significantly improve the chance of the plan being able to provide benefits to the remaining participants.

C. Additional Items

In addition to the corrections noted above, the ACLI believes that several additional items should be added to H.R. 2110 to clarify Congressional intent regarding the changes made by REA. These additions are as follows:

1. Clarification of Code Section 417(c)(2). REA Sections 103 and 203, amending Code Section 401(a)(11) and adding Code Section 417, should be changed to clarify Section 417(c)(2), the "Special Rule for Defined Contribution Plans". Currently, it is unclear whether 50% of a participant's account balance is a minimum to be applied to provide the qualified pre-retirement survivor annuity as otherwise determined by Section 417(c)(1), or if paragraph (2) applies in lieu of paragraph (1). Since applying only 50% of a participant's account (both vested and non-vested amounts) could result in a lesser death benefit for a

spouse than would have been required before REA, there can be a significant difference between the two interpretations.

2. Clarification of Code Section 417(f)(2). REA Sections 103 and 203, adding Code Section 417, should be changed to clarify Section 417(f)(2), which is the definition of annuity starting date. This paragraph provides: "The term 'annuity starting date' means the first day of the first period for which an amount is received as an annuity (whether by reason of retirement or disability)." Based on a literal reading of Section 417(f)(2) it is possible that, for participants who would receive lump sum payments, certain requirements of Section 417 might not be met because no "annuity" payment is made. A suggestion to prevent this is to add the words "or could be" following "for which an amount is". This change would also clarify the beginning date of the qualified joint and survivor benefit election period by effectively starting the election period 90 days before the earliest retirement age.
3. Modification of Code Section 417(a)(3)(B). Code Section 417(a)(3)(B) should be modified by deleting the words "preceding the plan year". As revised,

subparagraph (B) would read: "Each plan shall provide to each participant, within the period beginning with the first day of the plan year in which the participant attains age 32 and ending with the close of the plan year in which the participant attains age 35...." This would permit the notice and election procedure to occur at the same time, which would be administratively simpler and make it more likely that the participant would act upon the information provided.

4. Clarification of Code Section 411(a)(7). A change should be made to Code Section 411(a)(7) to clarify the status of a participant who separates from service without any nonforfeitable interest in the plan. Currently, it appears possible that unless there is an explicit cash-out, the forfeited funds associated with that participant cannot be made available to reduce employer costs. Yet, with a zero percent vested employee, no cash-out is possible--since nothing is owing to that individual by the plan.

To resolve this potential problem, we suggest that Code Section 411(a)(7) be modified to provide that a participant who separates from service with no vested interest would be deemed to have received a cash-out and his or her accrued benefit can be forfeited. Under

this rule, the participant will suffer no detriment so long as: 1) the plan is required to restore the forfeited amount if the participant is re-employed; and 2) the participant would have been able to additionally vest in the accrued benefit had he or she actually received a cash-out and repaid that cash-out upon such re-employment.

Another problem with this same section involves the right of a participant who has received a cash-out of his or her accrued benefit to have a forfeiture restored upon repayment of the cash-out. Prior to REA, Reg. Section 1.411(a)-7(d)(2)(ii)(D) provided that the right of repayment expired two years after the date of re-employment. To prevent any potential record-keeping and funding problems, we suggest that a provision be added to the Act to clarify that the pre-REA two year rule continues to apply to post-REA cash-outs.

5. Clarification of Code Section 411(a)(11). A provision should be added to the Act to clarify how to determine the present value of an accrued benefit for purposes of the Section 411(a)(11) restriction on mandatory distributions. Currently, subparagraph (B) of Section 411(a)(11) provides, in essence, that to determine the amount of present value to test against the \$3,500

threshold, the interest rate used may not be greater than the rate used by PBGC for determining the present value of a lump sum distribution at plan termination. The statute is not clear as to whether a plan may test the amount of present value using the PBGC rate, and then recalculate the present value using a different, perhaps higher, interest rate for the actual distribution.

This ambiguity could be resolved by striking the words "For purposes of subparagraph (A)," and replacing them with the words "Solely for purposes of determining the amount under subparagraph (A),".

6. Form of Annuity. A provision should be added to the Act to clarify that a spouse who is to receive a pre-retirement survivor annuity may elect a form other than a life income.

X X X X X X

We appreciate the opportunity to comment on H.R. 2110. If you need any additional information we will be happy to furnish it to you.

Respectfully submitted,

AMERICAN COUNCIL OF LIFE INSURANCE

LAW OFFICES

SANDERS, SCHNABEL & BRANDENBURG, P.C.

SUITE 600

1110 VERMONT AVENUE N.W.

WASHINGTON, D.C. 20005

TELEPHONE (202) 638 2241

CABLE LUCMER

TELECOPIER (202) 293 3419

TELEX ITT440356

June 7, 1985

JOHN A. SANDERS
ROBERT V. SCHNABEL
DAN S. BRANDENBURG
SUSAN PATRICIA FRANK
DAVID WEINGARTEN
JOHN J. ABBENE
ANDREW J. REINHARDT
DANIEL G. KAPLAN

* ALSO MEMBER OF MARYLAND STATE BAR
* ALSO MEMBER OF VIRGINIA STATE BAR
* ALSO MEMBER OF ILLINOIS STATE BAR
* ALSO MEMBER OF NEW YORK STATE BAR

LUCIEN H. MERCIER
1999 1967
N. MEYER BAKER
1909 1976

MARYLAND OFFICE
SUITE 600
5 MONROE STREET
ROCKVILLE, MARYLAND 20850

BERTIN B. SOYER
OF COUNSEL

HAND DELIVERED

Subcommittee on Labor-Management Relations
Committee On Education and Labor
U.S. House of Representatives
2451 Rayburn House Office Building
Washington, D.C. 20515

Attention: Ms. Phyllis Borzi
Pension Counsel

Dear Ms. Borzi:

On behalf of James J. Albertine, Director of Government Affairs, American Society of Association Executives, enclosed for the record are five (5) copies of Mr. Albertine's written comments on H. R. 2110, a bill making technical changes to the Retirement Equity Act of 1984 (P.L. 98-397).

Sincerely,

SANDERS, SCHNABEL & BRANDENBURG, P.C.

Dan S. Brandenburg
Dan S. Brandenburg

DSB/DW/JLL

Enclosures

cc: James J. Albertine

WRITTEN COMMENTS OF JAMES ALBERTINE,
DIRECTOR OF GOVERNMENT AFFAIRS OF THE
AMERICAN SOCIETY OF ASSOCIATION EXECUTIVES

The American Society of Association Executives ("ASAE") is pleased to have the opportunity to present its written comments for the printed record to the Subcommittee on Labor-Management Relations of the Committee on Education and Labor, U.S. House of Representatives on H.R. 2110, a bill making technical corrections to the Retirement Equity Act of 1984 ("REA").

ASAE is headquartered at 1575 Eye Street, N.W., Washington, D.C. 20005 (202-626-2703) and is the professional society for executives who manage trade and professional associations as well as other not-for-profit voluntary organizations in the United States and abroad. Founded in 1920 as the American Trade Association Executives with 67 charter members, ASAE now has a membership of over 11,000 individuals representing more than 6,500 national, state, and local associations. In turn, these business, professional, educational, technical and industrial associations represent an underlying force of more than 55 million people throughout the world. The overwhelming majority of ASAE's member represent tax-exempt organizations, most of which are either tax exempt as trade associations under Section 501(c)(6) of the Internal Revenue Code ("Code") or tax-exempt as educational or charitable organizations under Section 501(c)(3) of the Code. Many of ASAE's member associations sponsor qualified retirement plans for their members and their employees. As a result, ASAE is an interested party to legislative activity in this area.

H.R. 2110 addresses certain technical corrections in REA. ASAE believes that certain additional areas of REA require clarification.

I. Cashouts -

REA amended Section 411 of the Code (relating to minimum vesting requirements) to add a new Section 411(a)(11). The new Section provides as follows:

"(11) Restrictions On Certain Mandatory Distributions -

"(A) In General - If the present value of any accrued benefit exceeds \$3,500, such benefit shall not be treated as nonforfeitable if the plan provides that the present value of such benefit could be immediately distributed without the consent of the participant.

"(B) Determination Of Present Value - For purposes of subparagraph (A), present value shall be calculated by using an interest rate not greater than the interest rate which would be used (as of the date of the distribution) by the Pension Benefit Guaranty Corporation for purposes of determining the present value of a lump sum distribution on plan termination."

This provision, in ASAE's view, is unclear as to which PBGC interest rate should be used and for what purposes.

A. What rate applies -

The PBGC periodically issues a schedule of four interest rates depending on whether an immediate or deferred annuity is to be purchased. There are three deferred interest rates depending on the annuity commencement date of the participant. ASAE understands that many plans have, in the past, used the PBGC immediate annuity rate as the applicable PBGC interest rate in all situations. ASAE also understands that the PBGC would require a lump sum on plan termination to be valued based on the full range of PBGC interest rates. ASAE believes that a technical correction should be made to REA to clarify that the full range of PBGC interest rates is intended to be

used for purposes of Code Section 411(a)(11) and other Sections of the Code and ERISA that reference the PBGC interest rate for purposes of the \$3,500 cashout rule. This rule could also be used for purposes of determining present value under Section 2(c)(4)(A) of the bill (relating to payment to an alternate payee under a qualified domestic relations order).

B. For what purpose is the PBGC interest rate to be applied -

REA appears to limit the use of the PBGC interest rate to determine whether the consent of a participant to a cash-out must be obtained i.e. whether the amount of a benefit exceeds \$3,500. However, it has been suggested that REA also requires that the PBGC interest rate should also be used to determine the amount to be paid in a lump sum. ASAE believes this to be an unwarranted reading of REA. ASAE suggests that a technical correction to REA be adopted to clarify that the interest rate specified in a plan may be used to determine the actual amount to be distributed in a lump sum. This clarification is necessary to approve current plan practices and to avoid plans incurring additional costs in paying out lump sums. ASAE recognizes that there should be safeguards in the law to prevent a plan from using an unreasonably high interest rate. This will not affect the vast majority of plans that are using a range of rates, e.g. from 5% to 9%, that are reasonable.

C. Determination date -

Section 411(a)(11) of the Code, on its face, requires that a lump sum be valued as of the date of distribution for purposes of determining whether the consent of a participant to a cash-out must be obtained. The Senate Finance Committee Report provides that the PBGC interest rate as of the first day of the plan year in which the distribution occurs may be used

throughout the plan year if the plan so provides. ASAE believes that this is an important administrative rule. ASAE recommends that this rule be included as a technical correction to REA.

II. Minimum survivor annuity -

Section 2(b) of the bill would make several technical changes in the new survivor annuity rules added by REA. ASAE believes two additional clarifications are in order.

A. Pre-35 waiver of qualified preretirement survivor annuity -

REA requires that a waiver of the qualified preretirement survivor annuity be made during the "applicable election period". This term is defined in Section 417(a)(5)(B) of the Code, generally, as the period beginning on the first day of the plan year in which the participant attains age 35 and ending on the date of the participant's death. A participant's waiver is valid only if the spouse consents. It would appear that an election by a participant before the plan year in which the participant attains age 35 is invalid. Also, it would appear that while a participant must generally be at least 35 years old to waive this statutory death benefit, the spouse need not be 35 years or older to consent to such a waiver. In ASAE's view, it is unfair to prescribe by law that an adult cannot make a knowing and intelligent decision to waive his benefit before he is 35 years old. The consequence of this rule is that many young adults may be required to make a gift of monies received as a qualified preretirement survivor annuity to other members of their family to provide for the security of those family members. Unfortunately, this may result in adverse income and gift tax consequences that could otherwise have been avoided if the participant and his spouse would have been permitted to decide for themselves how the death benefit

should be payable. In this regard, ASAE would also suggest that a technical change to REA provide that a waiver of a qualified preretirement survivor annuity (or a qualified joint and survivor annuity) not be treated as a transfer of property for purposes of the gift tax rules under the Code. This can be accomplished by expanding the rule in Section 2(f)(1) of the bill, which now applies only to waivers by participants who perform service after January 1, 1976 and who separated from employment by August 23, 1984. Or this rule can be eliminated to avoid the negative implication that a waiver will result in a gift tax in all other similar situations. To avoid unnecessary problems such as this one, ASAE recommends that a technical correction to REA clarify that a waiver by a participant before he reaches age 35 (and the consent of his spouse at any age) is valid. Alternatively, if Congress determines that a permanent election cannot be made before age 35, a participant should be permitted to make a binding election before age 35 and should be required to make another election at age 35. Although, this additional step would create an administrative burden, it will enable adults, who in all other respects are able to make legally effective decisions, to control the disposition of their death benefit entitlement under the plan.

B. Form of payment of qualified joint and survivor annuity and qualified preretirement survivor annuity -

Code Section 417, added by REA, defines a qualified preretirement survivor annuity as a benefit in a specified amount payable as an annuity i.e. for the remainder of the life of the spouse. This form of benefit may be waived during the applicable election period. REA does not specify whether a participant (with his spouse's consent) or a spouse (upon the participant's

death) may elect that the statutory benefit be paid in the form of a lump sum. ASAE believes that it would be in the best interest of the surviving spouse to allow this death benefit to be paid as a lump sum. ASAE recommends that a technical correction to REA so provide.

ASAE would like to express its gratitude to the Subcommittee for the opportunity to submit its written comments on H.R. 2110.



AMERICAN SOCIETY OF PENSION ACTUARIES

Edward E. Burrows, Chairman
 Government Affairs Committee
 260 Bear Hill Road
 Waltham, Massachusetts 02154
 (617) 890-1780

June 4, 1985

Ms. Phyllis Borzi
 Pension Counsel
 Committee on Education and Labor
 U.S. House of Representative
 2451 Rayburn House Office Building
 Washington, D.C. 20515

Dear Phyllis:

Enclosed, are five copies of our statement respecting the DEFRA and REA Technical Corrections bills.

The first two sections deal with DEFRA, a subject which may or may not interest you. However, most of our comments did pertain to REA.

If there is any way we can help in pursuing these comments, we would like to do so. I'd be quite enthusiastic about discussing them with you either by telephone or in your office.

Sincerely,

Edward E. Burrows, Chairman
 Government Affairs Committee

cc: Chester J. Salkind
 Robert D. Levenson

Encls. (as stated)

jh

RECOMMENDED IMPROVEMENTS IN DEFRA AND REA
TECHNICAL CORRECTIONS BILLS

SUBMITTED BY THE
AMERICAN SOCIETY OF PENSION ACTUARIES
MAY 28, 1985

(The American Society of Pension Actuaries is a national professional society whose 2,000 members provide actuarial, consulting and administrative services to approximately 30% of the qualified retirement plans in the United States.)

A) SUGGESTED MODIFICATIONS OF DEFRA CORRECTIONS

1) The Pre-59½ Distribution Penalty Transition Provisions

Under the proposed bill, amounts attributable to contributions paid before January 1, 1985 are exempted from the penalty. The exemption should be changed so that it applies to amounts accrued before January 1, 1985. In the case of a defined contribution plan, this would include amounts actually credited as well as amounts with respect to which the employer's obligation to make the credit had become fixed. It would also apply to later adjustments for investment changes on these January 1, 1985 balances. Without these changes, the bill presents two administrative problems.

- a) Respecting defined contribution plans, it will be necessary to track forfeitures reallocated after January 1, 1985 and determine whether they are attributable to contributions made before that date.
- b) Respecting defined benefit plans, it is not clear what accruals are attributable to what contributions.

Our suggested modifications overcome both problems.

2) The 70½ Distribution Requirement for 5% Owners

The bill should provide clarification on these points:

- a) Is the 5% owner who reached 70½ long before DEFRA subject to the special distribution requirement?
- b) Consider the individual who is not a 5% owner at age 70½ but becomes one later. Is he subject to the requirement, and if so, when?
- c) Relative to effective dates, it should be made clear whether the first key April 1st is April 1, 1985, or April 1, 1986.

3) Definition of a Welfare Fund

The proposed bill attempts to provide "clarification" regarding circumstances in which an insurance company arrangement constitutes a welfare fund. The proposals do not reflect current practices regarding retentions and experience rating. Under these practices, the contract itself does not provide a guaranteed experience rating formula. However, the extra-contractual arrangement between the insurer and the contract-holder always assured that a formula will be followed. This distinction between form and practice should be recognized. The original intent of DEFRA will probably be best served if the proposed "clarification" is deleted.

B) DEFRA CORRECTIONS WHICH SHOULD NOT BE MADE

1) Repeal of IRC §2517

This proposal is substantive and does not appear to constitute an appropriate subject for a "technical corrections act." The proposed repeal would impact any irrevocable participant election of an annuity form which provides death benefits payable to a non-spouse. This tax treatment would apply at the time the election becomes irrevocable. This would be the case, for example, if a joint and survivor annuity were elected naming a non-spousal joint annuitant. §2517 probably should not be repealed even as part of a substantive tax act. What should be included is an amendment to §2517 exempting the employee's spouse as well as the employee. Without this amendment, there will be a gift whenever the spouse consents to an election away from spousal protection under §417.

2) Amendment of IRC §401(h)

The proposed change extending new restrictions to all key employees and not just 5% owners is also substantive and inappropriate for a "technical corrections act." There is no indication that DEFRA was unclear on the application of the new restriction. There is no indication that statutory language was in any way at odds with Congressional intent. It is not appropriate to justify the proposed change on the basis of bringing §401(h) into line with new welfare fund rules. The difference between the two sets of rules goes beyond the question of which employees are subject to the new separate account requirement. For example, the two sets of rules are different on the issue of unrelated business taxable income. They are different, as well, on the issue of reversion upon plan termination. Finally, they are different on the question of anticipating inflation.

C) SUGGESTED MODIFICATIONS OF REA CORRECTIONS

1) Status of Defined Contribution Qualified Pre-Retirement Benefits

There should be an acknowledgement that qualified pre-retirement death

benefits in defined contribution plans are fully subsidized whenever account balances are not forfeited upon death. It should also be acknowledged that §417 currently has some shortcomings in failing to deal with this particular type of fully subsidized death benefit. These rules should be considered for this fully subsidized benefit:

- a) The prohibition against opting out before age 35 does not apply.
- b) The requirements for notice and consent do apply. The notice requirement should provide for notice "within a reasonable period after the individual becomes a participant."

2) The Requirement to Use PBGC-Acceptable Interest Rates

This issue involves the rules on involuntary settlement of an amount whose value does not exceed \$3,500. The rule respecting PBGC-acceptable interest rates should only apply to determining whether a benefit is eligible for involuntary lump sum settlement. It should not apply to determining how much the settlement should be. Determinations relative to the amount of settlement should continue to be subject to the plan's basis of actuarial equivalence. To extend the PBGC-acceptable rate to determination of the amount will lead to discontinuities between lump sum settlements and other forms of settlements. These discontinuities will lead to such bizarre settlement forms as installments for two years certain.

If it is felt desirable to regulate plan definitions of actuarial equivalence more closely than at present, new rules should be carefully worked out and should be applied to all forms of settlement.

3) Amounts to Which the \$3,500 Test Applies

There is confusion regarding the amounts to be taken into consideration in applying the \$3,500 test.

These rules should be considered:

- a) The test is made after subtracting any non-vested amounts.
- b) Amounts subject to the test include mandatory employee contribution account balances.
- c) Amounts exclude voluntary employee contribution account balances.

4) Treatment of Lump Sum Settlements and In-Service Distributions for Spousal Consent Purposes

There is a good deal of uncertainty within the retirement plan community over whether lump sum settlements and in-service distributions are subject to spousal consent rules. This uncertainty should be eliminated either by statutory correction or by regulation. It seems clear that both transactions must be subject to spousal consent rules - assuming the profit-sharing exemption is inapplicable.

5) Restrictions on Deferred Annuities for Terminated Employees

Vested terminators from defined benefit plans which do not subsidize the pre-retirement spousal benefit represent very difficult administrative problems. In this and the next item, we are suggesting two avenues to elimination of these problems.

Under one avenue, a plan sponsor would be permitted to force the employee into a deferred annuity which includes a pre-retirement death benefit regardless of the former employee's marital status. The death benefit would ordinarily be the termination-time lump sum value of the deferred annuity plus interest to date of death. If the normal form of benefit did not include such a pre-retirement benefit, the terminating employee would find himself forced into a deferred annuity with a lower monthly payment than would have been the case under the normal form.

By providing that there is always a pre-annuity-commencement-date death benefit, the plan administrator sidesteps a difficult fact-finding problem. The problem is to determine, at the former employee's annuity commencement date, how much of the time between employment termination and the annuity commencement date the former employee had been married.

The point to be clarified in the technical corrections bill is that restricting vested terminators to deferred annuities which always include pre-retirement death benefits is not a cut-back. Before REA, the plan probably did not incorporate any such restriction.

6) Locking in the Vested Terminating Employee's Election at Time of Termination

In the preceding section, we suggested one method of avoiding a potentially difficult administrative problem relative to vested terminators.

A second method would be to freeze the employee's status at time of employment termination. If the employee made an election with spousal consent at time of employment termination, the spousal consent would never again be required, for any later change in election. This rule would apply whether or not the employee is married to the same spouse at time of annuity commencement. The employee who is single at time of employment termination would not be subject to spousal rules at any time thereafter. The employee who, at time of termination, is married and unable to obtain spousal consent would be forever locked into an annuity containing the pre-retirement death benefit. Furthermore, that death benefit would be related to the survivorship of the individual to whom the participant had been married at the time of termination.

7) Treatment of Non-Deductible Employee Contribution Account Balances

The proposed bill should be revised to clarify treatment of non-deductible employee contribution account balances relative to qualified pre-retirement death benefit provisions. Treatment appears clear in defined contribution plans: 50% of the account is subject to pre-retirement spousal benefit rules. Treatment is unclear in defined benefit plans.

One option is to apply defined contribution rules to the employee contribution account balance. There is an analogue for this approach in the application of §415 provisions.

The other option is to convert the account balance to an accrued benefit of the same form as the employer-financed accrued benefit. Then, the employee-financed accrued benefit would be added to the employer-financed benefit. Defined benefit spousal rules would be applied to the total.

This second option leads to differences in treatment of employee contribution account balances depending on the type of plan (defined benefit or defined contribution) of which they are part. The first option appears preferable.

8) Treatment of Employee Deductible Contribution Balances

The bill should clarify treatment of deductible employee contribution account balances relative to spousal annuity provisions. At present, these accounts appear subject to all spousal annuity rules. However, policy in the past has been to maintain consistency between treatment of these accounts and treatment of IRA account balances. Accordingly, we believe failure to exempt deductible employee contribution account balances from the spousal annuity requirements was an oversight which should be corrected.

9) Clarification of the 50% Rule

In a defined contribution plan, the qualified pre-retirement death benefit is defined by reference to "50% of the account balance." Most, but not all, defined contribution plans provide for full vesting of the account balance upon death. Many observers believe that for those plans which do not provide full vesting upon death, the 50% reference was intended to mean 50% of the vested balance. There should be clarification on this point.

10) Treatment of Loans

The proposed bill solves many of the problems imposed by REA when attempts are made to grant participant loans using vested interests as security. However, one problem left unsolved involves the participant who is unmarried at the time the loan is extended, but later becomes married. Loans made under this circumstance should receive the same protection as loans made before April 18, 1985.

11) Break In Service Rules - Elapsed Time Plans

Guidance should be provided relative to application of break in service rules to plans using elapsed time concepts. This guidance could take the form of statutory provisions. Alternatively, it could take the form of Congressional instructions, to Treasury, to publish regulations on the subject promptly. At present, this subject does not appear to be as high on the regulatory priority list as it should be.

12) Broadening of Gift Tax Exemption

In our discussion of DEFRA corrections, we raised objection to the repeal of §2517. We believe one of the REA corrections should involve extension of the exemption of §2517 to include a "gift" given by the participant's spouse who consents to an election away from spousal benefits.

13) Definition of Accrued Benefit

Attention should be given to the question of whether full subsidization of the qualified pre-retirement death benefit is part of the accrued benefit. For example, is full subsidization subject to the anti cutback rule?

For another example, suppose a vested terminator receives a lump sum settlement. Must the settlement include the value of the future pre-retirement spousal protection which would otherwise have been available? If so, must one consider the probability that a single employee will become married some time after employment termination?

It should be noted that depending on the answers to these questions, it may be necessary to amend definitions of actuarial equivalence to include marriage probabilities and marriage dissolution probabilities.

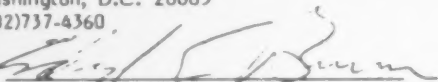
We suggest the position that full subsidization is not part of the accrued benefit for vesting and anti-cutback rules.

* * * * *

We would be eager to meet with members of the committees or their staffs to develop and clarify any of these recommendations.

American Society of Pension Actuaries
1413 K Street N.W.
Washington, D.C. 20005
(202)737-4360

by


Edward E. Burrows, M.S.P.A.

Chairman, Government Affairs Committee

jh



Suite 1000
1120 20th Street N.W.
Washington, DC 20036
Phone (202) 457-3838

Re: Recommended REA Technical Corrections

1. Waiver of Certain Distribution Requirements. H.R. 2110, Sec. 2(c)(4)(A)(v) modifies IRC Sec. 414(p)(9) by adding subparagraphs (A), (B), and (C). Subparagraph (9)(A) references IRC Sec. 401(a) in a manner that we find to be confusing. Sec. 401(a) does not appear to "prohibit payment of benefits before termination of employment," as is indicated by the reference in Sec. 414(p)(9)(A). One possible explanation is that the reference should have been to Sec. 401(a)(14), although that section focuses on when benefits must commence rather than upon a prohibition of commencement prior to termination.

As to the \$3500 limitation imposed by the amended IRC Sec. 414(p)(9)(B), this appears to be in conflict with ERISA Sec. 206(D)(3)(E). Sec. 206(d)(3)(E) of ERISA allows commencement of the alternate payee's benefit, if so specified under the terms of a qualified domestic relations order (QDRO), on or after the date participant's attainment of the earliest retirement age under the plan and allows an amount payable based on up to the present value of the accrued benefit of the participant as of the date of commencement of such payments.

In order to allow the early commencement of benefits provided under ERISA 206(d)(3)(E) and not limit such commencement to only those cases where the value of such early benefit is minimal, we would recommend deleting the H.R. 2110, Sec. (c)(A)(v) proposed paragraphs 9(B) and 9(C) (the latter describes determination of the present values to be used in 9(B)) for Sec. 414(p) of the Internal Revenue Code.

2. Elimination of Double Death Benefits. H.R. 2110 Sec. 2(f)(1) eliminates the double death benefit for a participant who dies during the transition period described in REA Sec. 303(c)(2).

We question the purpose of a correction limited to the transition period only, since the potential problem of "double death benefits" introduced by the joint and survivor annuity provisions of REA Secs. 103 and 203 extend beyond the transition period.

3. Federal Restriction on Garnishments. An additional point not addressed in REA or in H.R. 2110, is the intended effect of the Federal restrictions on garnishments upon the ERISA provisions concerning qualified domestic relations orders.

Section 206(d)(3)(A) of ERISA, as amended by REA, requires pension plans to provide for the payment of benefits in accordance with the applicable requirements of any QDRO. A QDRO is defined in part in Sec. 206(d)(3)(B) as a domestic relations order which "creates or recognizes the existence of an alternate payee's right to, or assigns to an alternate payee the right to receive all or a portion of the benefits payable with respect to a participant . . ." (emphasis added).

However, under 15 U.S.C. Sec. 1672(a) concerning garnishments, "pensions" are included in the definition of "earnings" and Sec. (c) of that part defines "garnishment" as "any legal or equitable procedure through which earnings of any individual are required to be withheld for payment of any debt."

15 U.S.C. Sec. 1673(a) restricts the maximum garnishment to 25 percent of disposable earnings or the amount by which disposable earnings for the week exceed thirty times the Federal minimum hourly wage, whichever is less. Exceptions to this restriction are under 15 U.S.C. Sec. 1673(b) which provides that "the maximum part of the aggregate disposable earnings of an individual for any workweek which is subject to garnishment to enforce any order for the support of any person shall not exceed (50 to 65 percent, depending upon other support obligations specified)."

If domestic relations orders are within the garnishment definitions, then it would appear that in no case could "all" of a pension be assigned to an alternate payee unless the participant had additional earnings, and Sec. 206(d) of ERISA should be amended to provide specifically that amounts assigned under a QDRO may not exceed garnishment restrictions.

If domestic relations orders are not within the garnishment definition, Sec. 206(d) of ERISA should be amended to clearly state that QDROs are not subject to the garnishment restrictions. In such case, guidance on whether a court order which is labeled a "garnishment" and which otherwise meets the requirements of a QDRO would be acceptable as a QDRO. (This

would arise, for example, where the participant defaulted in alimony payments which were originally ordered to be made by the individual, not the plan.)

4. Joint-Survivor Annuity Election Period. ERISA Sec. 205(c)(6)(and IRC Sec. 417(a)(5)), concerning the election period for a joint and survivor annuity, now specifies that the election period is ". . . the 90-day period ending on the annuity start date . . ."

If this provision is applied in instances where the employment termination date is immediate, whether due to the requirements of the company or the employee's election, there would not be adequate time for the employee involved to reach a decision concerning the survivor annuity. It would appear that any waiver of the survivor annuity executed subsequent to the annuity start date could be found to be invalid under the above terms.

Prior to REA, IRC Reg. 1.401(a)-11(c). (ii) allowed ". . . at least 90 days following the furnishing of all of the applicable information . . ." and provided for an extension of the 90 days for an additional 90 days if additional information was requested by the participant.

If the intent of REA was to continue the prior and more liberal practice, we feel that the following wording should be substituted as a technical correction:

205(c)(6) For the purposes of this subsection, the term "applicable election period" means -

(A) in the case of an election to waive the qualified joint and survivor annuity form of benefit, the 90-day period ending on the later of the annuity starting date or the ninetieth day following receipt by the participant of all applicable information including the cost of this form of benefit, or

(The same wording would be used in IRC Sec. 417(a)(5).)

5. Domestic Relations Orders. Section 206(d)(3)(D), dealing with QDRO's, specifies that "A domestic relations order meets the requirements of this subparagraph only if such order does not require a plan to provide any type or form of benefits, or any option, not otherwise provided under the plan . . ."

Certain orders for support and back support payments anticipate an ending date of "after x years" or "after y amount of money has been paid." These are effectively temporary annuities or annuities for a stated term. Plans which provide only a joint life annuity or a single life annuity apparently would be obligated to reject such orders or risk having unlawfully alienated benefits.

Prior to REA, Revenue Rule 80-27, case law (American Telephone and Telephone Co. v. Merry, 592 F. 2d 118 (2nd Cir. 1979)) and various private letter rulings indicated that the anti-alienation provisions of ERISA were not meant to apply to alimony and support payments as long as the pension involved was in pay status at the time such payments were made.

If REA is to expand upon and not limit the foregoing, we feel that the proper solution would be addition of the following language as a technical correction:

206(d)(3)(D)(i)(I) In the case where payments to the alternate payee are of a specified duration of a temporary nature and the normal form of benefit under the plan is a single or joint life annuity, a domestic relations order shall not be treated as failing to meet the requirements of clause (i) of this subparagraph to the extent that such payments are in pay status to the participant at the time payments to the alternate payee are to begin and are specified in the order to end on the earliest of: completion of the specified duration, payment of the specified amount, the death of the alternate payee or the death of the participant. For purposes of this subclause, subparagraph (E) of this section shall not apply.

The purpose in eliminating the early commencement provision (subparagraph (E)) is to remain consistent with Sec. 206(d)(3)(D)(ii), which prohibits a domestic relations order from requiring a plan to provide increased benefits. This would occur if, for example, a back support award of a specified dollar amount were paid to the alternate payee prior to the retirement of the participant and the participant dies prior to retirement. No actuarial reduction could be taken from the alternate payee, since a set dollar amount was awarded; no actuarial reduction could be taken from the participant, since no pension payments were made.

6. Defined Contribution Plan Payouts. IRC Sec. 411 (Minimum Vesting Standards) provides that an employee's accrued benefit under a qualified plan must become nonforfeitable at least as quickly as under the minimum standards. For purposes of the minimum vesting rules, the term "accrued benefit" means:

(i) in the case of a defined benefit plan, the employee's accrued benefit determined under the plan. . . expressed in the form of an annual benefit commencing at normal retirement age, or

(ii) in the case of a plan which is not a defined plan, the balance of the employee's account. (Sec. 411(a)(7))

The REA added Sec. 411(a)(11) which provides that "if the present value of any accrued benefit exceeds \$3500, such benefit shall not be treated as nonforfeitable if the plan provides that the present value of such benefit could be immediately distributed without the consent of the participant." This restriction on immediate payouts applies to both defined benefit and defined contribution plans.

Under the AT&T Savings Plans, the AT&T ESOP, and the AT&T Voluntary Contribution Plan, employees who terminate employment generally receive an immediate distribution of their accounts. In the case of the Savings Plan and the Voluntary Contribution Plan, but not ESOP, only employees who retire on a service pension or are disabled may elect to defer the distribution of their accounts.

The AT&T Pension Plans provide for deferred vested pensions to participants who terminate with at least 10 years of service (if the present value of the accrued benefit exceeds \$3500). But the extension of the right to deferred payouts to all employees who terminate employment under the AT&T defined contribution plans could reach participants with as little as one or two years of service (as long as the nonforfeitable account balance exceeded \$3500). This extension creates a tremendous burden on the plans to maintain the separate accounts of these terminated participants for years into the future. Since these plans were never intended to provide for deferred payment of benefits (except in limited circumstances) we urge the adoption of a technical correction to limit the requirements of Sec. 411(a)(11) to plans which provide life annuities as the normal form of benefit.

APPWP

Association of Private Pension and Welfare Plans

Stuart J. Brahs
Executive Director

June 12, 1985

Honorable William Clay
Chairman, Subcommittee on
Labor-Management Relations
Committee on Education and Labor
U.S. House of Representatives
2451 Rayburn House Office Building
Washington, D.C. 20515

Attn: Phyllis C. Borzi, Esquire
Pension Counsel

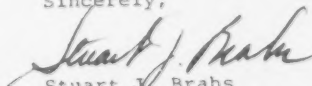
Dear Mr. Chairman:

The Association of Private Pension and Welfare Plans (APPWP), in response to your May 16 announcement, appreciates this opportunity to comment on H.R. 2110, a bill making technical changes to the Retirement Equity Act of 1984 (Public Law 98-397).

It is to be hoped that the attached statement will assist your Subcommittee in its consideration of this legislation. Should you have any questions or desire any additional comments from the APPWP on this issue, it is to be hoped that you will not hesitate to call on us.

Best regards,

Sincerely,


Stuart J. Brahs
Executive Director

SJB:sr

Enclosures (5)

Introduction

This statement is submitted on behalf of the Association of Private Pension and Welfare Plans ("APPWP"). APPWP is a nonprofit organization, founded in 1967 to foster the growth of employer-sponsored group employee benefits systems. APPWP represents over 475 organizations throughout the United States, including large and small employers who sponsor plans, as well as leading support organizations to private plans, such as banks, insurance companies, and accounting, actuarial and consulting firms. Collectively, the APPWP membership is involved directly with virtually all employee benefit plans.

We welcome the opportunity to comment on H.R. 2110. When enacted in 1984, the Retirement Equity Act ("REA") raised a number of technical questions and uncertainties. While many of these issues could be resolved through regulations and pronouncements of the Department of Treasury, APPWP believes that difficult technical issues are more appropriately left to the purview of Congress. Moreover, Treasury regulations and rulings frequently lag years behind the enactment of a new law. Although we are aware of the difficulties inherent in the rapid issuance of regulations, pension plan sponsors and service providers are subject to ambiguous new laws long before such guidance is available. Thus, APPWP commends and supports this Committee's work on technical correction bills. APPWP believes that this effort will give Congress the opportunity to

make necessary clarification in the law with public input and full consideration of the competing concerns raised by these issues.

Considerations

Before discussing our specific concerns with the technical corrections bill, we wish to note generally that, while we believe many of the provisions of the bills serve to clarify REA, it appears that some provisions would make substantive and non-technical changes to the Internal Revenue Code (the "Code") and Title I of the Employee Retirement Income Security Act of 1974 ("ERISA"). Recognizing that the line between technical and substantive changes is often fine, we nonetheless urge the Committee to avoid creating still another set of substantive changes in the laws governing employee benefit plans without full congressional consideration of the ramifications.

Our specific concerns with H.R. 2110 fall into three categories. First, we are troubled by the proposed retroactive application of several of the technical corrections, and we recommend that Congress closely analyze whether technical corrections in this area should be retroactive. Second, there are a number of important areas which have been totally ignored by H.R. 2110, which, we feel, merit congressional consideration. Finally, some of the issues treated in the bill remain vague and confusing, and should be refined before final adoption.

Retroactive Effect

Certain of the retroactive effective dates in H.R. 2110 cause enormous confusion, and, if enacted unchanged, will create hardship on plans and participants. For example, the amendments to the qualified domestic relations orders provision in Code Section 414(p) have retroactive effective dates which could result in the inadvertent disqualification of a plan because of conduct taken in good faith on the basis of a vaguely drafted section of the law.

Issues Not Considered by H.R. 2110

Our second area of concern relates to the many difficult issues under REA which have not been clarified in H.R. 2110. For example, there are several unresolved questions about the joint and survivor and pre-retirement spousal death benefits. REA revised section 401(a)(11) of the Code to require that the benefits of a married, vested participant be payable in the form of a joint and survivor annuity and a pre-retirement spousal annuity. The provision applies to all plans except stock bonus and profit sharing plans which meet the requirements of section 401(a)(11)(B)(iii). Various issues relating to this exception are unresolved. Specifically, Congress should clarify whether the exception is available to otherwise qualifying plans which accept rollovers from non-qualifying plans (as distinguished from plans which accept plan-to-plan transfers), and whether, with respect to a plan

falling within the exception, the requirement for spousal consent to an alternative beneficiary may be waived if the participant establishes that his spouse is unavailable. In addition, there is continuing confusion as to whether or not spousal consent is required for in-service withdrawals or loans from plans that meet the section 401(a)(11) exception. (Similarly, although H.R. 2110 would require spousal consent as to loans and withdrawals from plans which do not come under the exception, there is no guidance as to how a plan should deal with those loans made prior to H.R. 2110 without spousal consent.)

Also unresolved are certain questions about the revocability of spousal consents. While H.R. 2110 provides for automatic revocation of spousal consent to a waiver of the pre-retirement spousal death benefit if a new beneficiary is selected, no similar provision is made with respect to waivers of the joint and survivor annuity. For instance, H.R. 2110 does not clarify whether or not a spouse who has consented to a waiver of the joint and survivor benefit may ever revoke his consent. In this connection, is a plan required to deem revocation of consent if the participant in some way changes his election (e.g., by changing his selected benefit payment form from a single life annuity to a lump sum)?

Other open issues pertain to the cash-out provisions. Regardless of the participant's or spouse's election, section 417 permits plans to make cash-outs of the joint and survivor benefit or the pre-retirement spousal benefit if the

value of the benefit does not exceed \$3500. For purposes of determining the \$3500 amount, it is unclear whether a plan administrator is expected to look only to the benefits derived from vested employer contributions, or whether employee contributions are to be considered as well. Also, if an in-service withdrawal is made, should the amounts withdrawn be counted in determining the \$3500 threshold? Similarly, under section 401(a)(11), the joint and survivor and pre-retirement spousal death benefits applies with respect to those participants who have a vested interest in their benefits; is a participant who has vested in no portion of his employer-derived benefit, but has a vested employee contribution benefit in excess of \$3500 exempt from the joint and survivor and pre-retirement spousal death benefit coverage?

In the event that the value of the joint and survivor or pre-retirement spousal death benefit exceeds \$3500, section 417 states that a plan may allow for an immediate cash-out of the benefit, provided that the participant and his spouse (or, where the participant has died, his surviving spouse) consent to such a distribution. It is not clear whether a spousal consent made under these circumstances must satisfy the requirements of section 417(a)(2)(A), which requires written consent, witnessed by a plan representative or notary public.

Also, as currently drafted, the joint and survivor and pre-retirement spousal death benefits appear to apply to all benefits, including disability benefits. However, in drafting their plans to conform to REA, plan sponsors are

uncertain as to whether so-called social security, lay-off or early retirement subsidies (e.g., subsidies which increase benefits for a specific term) are also subject to the joint and survivor and pre-retirement spousal death benefits.

Under section 417, each plan (except those described in section 401(a)(11)(B)(iii)) must provide a participant the right to waive the pre-retirement spousal death benefit and to revoke the waiver during the applicable election period; if the plan does not subsidize the benefit (i.e., failure to waive the benefit will reduce the participant's benefit), the plan administrator must provide the participant with a written explanation of the terms and conditions of the pre-retirement spousal death benefit between the plan years in which the participant attains age 32 and 35 (or, under H.R. 2110, a reasonable period after hire).

When drafting plans to conform to these requirements, plan sponsors have encountered some difficulties. First, if the plan fully subsidizes the pre-retirement spousal death benefit, and offers no alternative death benefit, must a plan provide for waiver of the benefit (since it would be economically imprudent for a participant to waive the benefit)? We believe that if the waiver language is required to be included in the plan under such circumstances, no purpose would be served by including the provision since there would be no requirement that the participant be notified of the ability to waive. We suggest, therefore, that such plans be exempt from the requirement that they contain waiver language. Second, it

has come to our attention that several plans subsidize the death benefit to participants who die while employed, but do not subsidize the death benefit of a participant who terminates from service before his death: in such cases, we question whether it is appropriate to give notice to employees between the ages of 32 and 35 and believe that it would be more practical to give notice upon the participant's termination. We believe that these issues could be readily clarified through minor technical refinements.

Also, H.R. 2110 does not deal with the confusion caused by Code section 411(a)(11) which prohibits the mandatory cash-out of lump sum benefits if the present value of such benefits exceeds \$3500 without the participant's consent. First, it is unclear whether, for purposes of determining the \$3500 amount, the plan need look only at the present benefit, or whether previously withdrawn amounts (or amounts subject to a qualified domestic relations order) must also be taken into account. Second, it is unclear what constitutes consent for purposes of section 411(a)(11). For example, would a plan satisfy the requirements of section 411(a)(11) if it provided that a participant's benefits could be immediately distributed in the event that the participant failed to make a contrary election within a given time period? Would such consent have to be signed or witnessed? Third, when drafting a plan to conform to this requirement, plan sponsors are uncertain as to how long a participant may elect to defer benefit commencement,

i.e., would a plan be able to provide for a mandatory distribution upon the participant's attainment of normal retirement age, or would the plan have to permit deferral until the section 401(a)(9) required date? Finally, following the enactment of section 411(a)(11), may a plan continue to provide a lump sum distribution as the sole distribution form?

The rate used for cash-outs is similarly uncertain. Although the statute makes clear that a rate no greater than the Pension Benefit Guaranty Corporation's rate for determining the value of a lump sum distribution on plan termination must be used, it is not clear when that rate is to be used. The statutory language of REA suggests that the PBGC rate is to be used only to determine whether the threshold of \$3500 is met, and not for the actual valuation of the cash-out, which is properly calculated using plan rates and factors adopted pursuant to Code section 401(a)(25). Informally, however, the Treasury takes a contrary view, mandating the use of PBGC rates for all purposes. This lack of clarity may create liability for plan sponsors.

An additional area omitted from H.R. 2110 relates to the application of the anti-cutback rule to terminated plans. The statute offers no guidance with respect to the obligations of an insurer that issues irrevocable commitments to participants in a terminating plan in accordance with the requirements of Title IV of ERISA, nor has Treasury guidance been forthcoming.

In addition, following the amendment to Code section 411(d)(6), insurers can not be certain as to how to value benefits to be provided after plan termination, since a participant who meets the conditions of a benefit subsidy after plan termination must be provided that subsidy. The insurer will inevitably be obligated to price the annuity as if all conditions will subsequently be met. Such a course could conceivably deplete plan assets which might otherwise be applied to other lower priority benefits under the plan, and could cause an otherwise sufficient plan under Title IV to become insufficient and therefore trustees by the PBGC, rather than closed out in the private sector. In addition, this rule requires that the plan sponsor continue to keep records of service for participants who have not satisfied the conditions for the subsidy, as if the plan had not been terminated.

The new vesting provisions have also given rise to some confusion. For example, if a participant terminates service within 5 years of normal retirement date, leaving his vested and unvested amounts in the plan, will his nonforfeitable benefits be subject to forfeiture under the new provisions (or will he automatically vest upon his normal retirement date)?

Questions Raised by the Technical Corrections

Our third area of concern is that the technical corrections bills, as adopted, will create new confusion. For example, the change in H.R. 2110, which prohibits the cash-out

of a divorced spouse's benefits in excess of \$3500, is, in our view, ill-considered. Code section 414(p), as added by REA, appeared to permit a divorced spouse's benefit to be cashed out, subject to the general rules elsewhere in the Code with respect to consent. This rule would have vastly increased the recordkeeping of the plan where spousal consent could not be obtained. The "clarification" in H.R. 2110, which was purportedly intended to ease the burden on plan administrators, does not even begin to recognize the added burden caused by these additional account balances. Moreover, there appears to be no valid reason to treat payments to divorced spouses in the same manner as payments to participants. The domestic relations order provisions were intended to facilitate property settlements; they were not intended to create a new class of participants in divorced spouses and grant these individuals equal substantive pension rights. Moreover, it is not clear how amounts subject to qualified domestic relations orders are to be treated: is the amount payable to each spouse tested separately to determine if it exceeds the \$3500 cash-out threshold or must the amounts be aggregated for this purpose? APPWP takes the position that, unless these amounts are tested separately, the burden on plan administrators is needlessly multiplied.

A further problem created by language in the technical corrections bills arises as a result of the way the proposed changes in H.R. 2110 on spousal consent relate to the proposed repeal of Code section 2517 under H.R. 1800. Under

Code section 2517, the exercise or nonexercise of an election or option under a qualified plan is not considered a transfer for gift tax purposes. By repealing this provision, H.R. 1800 may cause the imposition of gift tax liability each time a beneficiary designation has been made or recorded. This proposed amendment makes little sense in light of the new spousal consent provisions of REA. Moreover, it is not clear upon whom the liability would fall: if Code section 2517 is repealed, participant designations in favor of a beneficiary other than a spouse may result in gift tax to either the participant or the spouse who consents to waive the REA-required spousal annuity. This question is especially difficult in light of the provision of H.R. 2110 which requires the spouse's waiver to acknowledge that the death benefit will be paid to a specific alternative beneficiary.

**BUCK
CONSULTANTS**

Two Pennsylvania Plaza
New York, New York 10121 212 279 4400

June 7, 1985

Honorable William Clay, Chairman
House Education and Labor
Subcommittee on Labor-Management Relations
2451 RHOB
Washington, D.C. 20515

Re: H.R. 2110 - The REA Technical Corrections Act

Dear Mr. Clay:

Buck Consultants, Inc., as one of the nation's leading employee benefits firms, has analyzed H.R. 2110, a bill that purportedly makes only technical corrections to the Retirement Equity Act of 1984 (REA). We are concerned that H.R. 2110 would require many employers to make additional substantive changes in their retirement programs. Moreover, while adding new administrative burdens, some ambiguities and problem areas of REA have not been clarified.

Our comments on some of the substantive features of H.R. 2110 are as follows:

- In the area of employee taxation, we strongly object to H.R. 2110's harsh provision that would retroactively disqualify the favorable lump sum tax treatment accorded to a plan participant who upon reemployment has a previous forfeiture restored and vested. It should be noted that the original distribution was the entire amount available to the employee at the time it was made. The socially desirable rules for restoring forfeitures upon reemployment and permitting employees to vest in the restored amounts would be negated if the tax consequences serve to discourage reemployment.
- A new administrative burden would be created by requiring the spouse's consent before a married participant could take a loan from a plan using the accrued benefit as collateral. This impediment to loans would be required under all qualified plans that are covered by REA's preretirement survivor annuity provisions.

Buck Consultants, Inc.

George B. Buck Consulting Actuaries, Inc. | Buck Pension Fund Services, Inc. | Buck Research Corporation | GBB Associates, Ltd.

Plans have an 18-month period to determine if a Domestic Relations Order (DRO) is qualified. However, one of the requirements for qualification is precision concerning the starting date of the benefit payment. H.R. 2110 generally extends the time for determining qualification by stating that the 18-month period commences on the benefit payment date stipulated in the order. We agree that it would be desirable to defer the 18-month period for the determination of whether a DRO is qualified. However, in those cases in which the DRO does not specify the starting date for benefit payments, we recommend that the 18-month period commence no earlier than the employee's earliest possible retirement date.

Lump sum payouts in accordance with a Qualified Domestic Relations Order would be limited to \$3,500. We believe that the alternate payee and the plan administrator would generally benefit from the removal of this limit. Therefore, we recommend that the limit be removed. If, however, the limit is retained, it would seem to be an unduly harsh penalty to disqualify a plan in situations where the limit is inadvertently exceeded.

In addition, we believe that H.R. 2110 should address the following areas:

- . The law should explicitly permit involuntary lump sum distributions in excess of \$3,500 from a defined contribution plan other than a pension plan upon termination of employment.
- . The minimum age of 35 for electing out of preretirement survivor annuity coverage should be removed. Any employee, whether above or below age 35, who meets the conditions for preretirement survivor annuity coverage should be permitted to submit a waiver if the plan imposes a charge for this coverage.
- . A married vested participant who has been abandoned by his/her spouse for a specified period but is not legally separated should be treated for qualified joint and survivor annuity and preretirement survivor annuity purposes as if he/she was single.

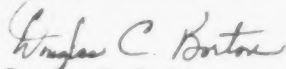
Conclusion

We at Buck agree that the Retirement Equity Act requires technical amendment. However, H.R. 2110 ignores those problems which we have noted.

We hope these comments are helpful in your analysis of H.R. 2110. If you have any questions, we would be happy to be of further assistance.

Very truly yours,

BUCK CONSULTANTS, INC.



Douglas C. Borton
Chief Actuary

DCB:AA

cc Honorable Dan Rostenkowski, Chairman, House Ways and Means Committee
Honorable Bob Packwood, Chairman, Senate Finance Committee
Honorable Don Nickles, Chairman, Subcommittee on Labor, Senate Labor
and Human Resources Committee
Mr. Ronald A. Pearlman, Assistant Secretary Tax Policy, Department of
Treasury

LAB OFFICES
GROOM AND NORDBERG
CHARTERED

SUITE 700

1775 PENNSYLVANIA AVENUE, N.W.
WASHINGTON, D.C. 20006

(202) 857-0620
TELEX 202 659 4503

HOWARD J. GILBERTSON
DIRECTOR

THEODORE R. GROOM
CARL A. NORDBERG, JR.
ROBERT B. HARDING
LAWRENCE J. HART
LOUIS T. MAZAR
MICHAEL E. KELLER
JENNIFER BRICE
DAVID M. FORD
DANIEL HOROWITZ
STEPHEN M. DAYON
ROBERT F. GALLAGHER
DOUGLAS A. ELL
WILLIAM T. WERNER
MARK A. MAJESTER
TERENCE M. DENYEN
JUSTIN L. MONT
MARY BAILEY LUND

ADMITTED IN A.D.C.
ADMITTED IN A.D.C.

May 29, 1985

The Honorable William L. Clay
Chairman
Subcommittee on Labor-Management Relations
U.S. House of Representatives
2451 Rayburn House Office Building
Washington, D.C. 20515

Re: Comments on H.R. 2110 on Behalf
of Chevron Corporation

Dear Mr. Chairman:

These comments on H.R. 2110, a bill to make technical corrections to the Retirement Equity Act, are submitted on behalf of Chevron Corporation ("Chevron"). Chevron and its affiliates (including Gulf Oil Corporation) currently maintain tax-qualified plans for the benefit of over 90,000 employees, former employees, and their beneficiaries.

Our comments may be briefly summarized as follows:

1. Where an alternate payee is entitled to benefits under a qualified domestic relations order ("QDRO"), plans should be permitted to distribute benefits at any time without adversely affecting their tax-qualified status if the plan provides for, and the alternate payee consents to, the distribution.

2. The relationship between the survivor benefit rules and the QDRO provisions should be clarified by statute. In particular, it should be confirmed that the joint and survivor rules, and the related requirement for exempted plans that 100 percent of the account balance be payable upon the participant's death to the surviving spouse, do not apply to the extent benefits have been assigned to an alternate payee by a QDRO.
3. It should be confirmed that, should an alternate payee choose to receive benefits where the participant continues working and is not fully vested, the plan is not required to increase benefits to the alternate payee to reflect subsequent vesting by the participant.
4. The Federal income and gift tax consequences of spousal waivers of benefits should be clarified.
5. The expanded spousal consent rules should also be clarified, particularly (1) with respect to the requirement that consent apply to a specific beneficiary and (2) to deal with plans which generally do not provide for payments to other beneficiaries where the spouse consents to waive survivor coverage.
6. The transition rule to avoid double death benefits should be revised or eliminated, to remove any implication that double benefits are required outside the scope of the rule.
7. The tax consequences of QDRO payments to alternate payees other than former spouses should be clarified.

These comments are set forth more fully below.

1. Where the Alternate Payee Consents and the Plan So Provides, Plans Should Be Permitted To Cash-Out or Commence Benefits Under a QDRO at Any Time, and Unilateral Cash-Outs of Small Benefits Should Be Permitted

Sections 104 and 204 of the Retirement Equity Act provide an exception to ERISA's assignment, alienation, and

preemption provisions for the payment of plan benefits to an alternate payee pursuant to a qualified domestic relations order ("QDRO"). The basic purpose of these provisions was to allow state courts to divide benefits in connection with divorce, subject to certain safeguards designed primarily to minimize the burdens and potential liabilities of plans and plan administrators. One such safeguard prevents a state court from ordering a plan to commence payments to an alternate payee prior to the date the participant attains or would have attained the plan's earliest retirement age. Code §§ 414(p)(3) and (4). In our view, this safeguard by itself does not limit a plan's ability, if it so desires, to commence payments at an earlier date.

There are general restrictions under Code sections 401(a) and 401(k), which apply to some but not all tax-qualified retirement plans, on the payment of benefits prior to termination of employment.^{*/} The last sentence in Code section 414(p)(5) states that these restrictions do

^{*/} Regulation section 1.401-1(b)(1)(i) has been interpreted to prohibit a defined benefit or money purchase pension plan from making in-service distributions prior to a participant's attaining normal retirement age. See T.I.R. 1403, Q&A M-15; IRS Letter Ruling 8453082 (Oct. 3, 1984). Code section 401(k)(2)(B) generally prohibits a qualified cash or deferred arrangement, which may be part of a profit-sharing or stock bonus plan, from making in-service distributions prior to a participant's attaining age 59-1/2.

not apply to payments to an alternate payee "pursuant to a qualified domestic relations order." While we believe that this sentence was intended broadly to avoid any violation of sections 401(a) and 401(k) where payments are made to an alternate payee, the sentence could be read to avoid a violation only where the QDRO itself specifically authorizes the payment at that time.

Section 2(c)(4)(A)(v) of H.R. 2110 is intended to address the extent to which the sections 401(a) and 401(k) restrictions apply to payments to an alternate payee prior to any date specifically set forth in the QDRO. The proposed solution is that the restrictions would apply unless the present value of such payments does not exceed \$3,500. As presently worded, the restrictions would not be waived for larger amounts, even if immediate payment is desired by the alternate payee.

In testimony before the Ways and Means Committee on May 16, the Treasury Department suggested that the issue of whether payments may be made to an alternate payee before the participant terminates employment should not be decided on the basis of the present value of the payments. We agree. We also agree that divorce "effectively severs" the link between the alternate payee and the employer maintaining the plan, and "thus may be seen as functionally equivalent to a participant's separation from service."

In our view, the proposed sweeping restriction on payments to alternate payees is contrary to the intent of the Retirement Equity Act. It was in recognition of the possible need of a divorced spouse for immediate funds that the "earliest retirement age" exception was added. Because the exception allows a court to order payments to an alternate payee even if not provided for under the plan, the condition that the participant attain the earliest retirement age was added to minimize the administrative burdens placed on plans. Where a plan and the alternate payee both desire earlier payments, we believe the statutory purpose is further served by facilitating, rather than prohibiting, such payments.

We recommend that this distribution of benefits issue be resolved in a manner which reasonably accommodates the needs of divorced spouses and the administrative problems of plan administrators. In the case of surviving spouses of deceased participants, the solution adopted by the Retirement Equity Act to balance these needs and problems is a \$3,500 rule: benefits with a present value greater than \$3,500 may be cashed-out only with consent, and benefits with a present value not greater than \$3,500 may be cashed-out at the plan's discretion. We believe that

similar rules should apply to surviving spouses and divorced spouses, and that the \$3,500 compromise of the Retirement Equity Act should be extended to divorced spouses.*

To summarize our views on this issue, we recommend that H.R. 2110 be revised to provide as follows:

1. The restrictions under Code sections 401(a) and 401(k) regarding the payment of benefits prior to the termination of employment do not apply to payments to an alternate payee under a QDRO, regardless of when made, if the plan provides for such payments.
2. Where the present value of payments to the alternate payee exceeds \$3,500, such payments may be cashed-out only with the consent of the alternate payee.
3. Where such present value does not exceed \$3,500, payments may be cashed-out at the discretion of the plan administrator.
4. Present value should be determined as of the date of receipt of the QDRO by the plan.

*/ Code § 417(e). While we believe that similar rules should apply to surviving spouses and divorced spouses, we would emphasize that there is an urgent need for clarification of the scope of Code section 417(e) and the related rules of Code section 411(a)(11).

We note two differences between our recommendations above and the testimony of the Treasury Department. First, we urge that the administrative costs and burdens created by small benefits be recognized, and that the \$3,500 cash-out rule of the Retirement Equity Act be expanded to include QDRO payments. Second, the Treasury statement seems to suggest that the Code sections 401(a) and 401(k) restrictions would not apply only where the QDRO itself authorizes payments prior to the termination of employment. In that event, because a QDRO may not order payments to be made prior to the participant's attainment of the earliest retirement age, payments to the alternate payee prior to that time might violate sections 401(a) or 401(k) if the participant remains in service.

These apparent limitations fail to recognize that the policy underlying the cash-out rules applies whenever a plan is confronted with the task of accounting for benefits, particularly small benefits, with respect to individuals who are no longer connected with the employer or the plan. Specifically, the cash-out rules recognize that it may be exceedingly difficult for plans to maintain current information regarding the whereabouts of such persons. This problem is particularly acute for defined contribution plans that provide for directed investments and where there may be a need for regular contact with

alternate payees with respect to investment matters. We would emphasize also that rules which provide plans with reasonable flexibility to deal with these problems through cash-outs will not prevent alternate payees from preserving their funds for retirement purposes, because (1) Code section 402(a)(6)(F) expressly allows tax-free rollovers of amounts received under QDROs and (2) plan administrators are required under Code section 402(f) to notify recipients of opportunities to make such rollovers. Accordingly, we believe that the sections 401(a) and 401(k) restrictions should not apply to QDRO payments whenever made, and that the divorced spouse's interests are adequately protected if written consent is required to cash out benefits exceeding \$3,500.

2. The Relationship Between the Survivor Benefit Requirements and QDROs Should Be Confirmed in the Statute

Sections 103 and 203 of the Retirement Equity Act generally require that a preretirement or post-retirement survivor annuity be paid to the spouse of a deceased vested participant, unless the spouse consents in writing to waive the benefit. Certain profit-sharing and stock bonus plans are generally exempted from these survivor benefit requirements, but only if 100 percent of the account balance will

be paid to the surviving spouse upon the participant's death (unless the spouse consents otherwise).

One very important question in this area is as follows. Where a QDRO assigns a portion of a participant's accrued benefit to a divorced spouse or other alternate payee, and the participant remarries and then dies, are the benefits assigned by the QDRO to the first divorced spouse excluded for purpose of computing the survivor benefits payable to the second spouse? Although the statute does not address this important issue, we think the legislative history makes it clear that a plan is not required to pay the same benefit twice, *i.e.*, to both spouses. The final Senate Report on the Retirement Equity Act states that:

"This rule [presumably referring to the general joint and survivor rules] does not apply, however, if a qualified domestic relations order . . . otherwise provides for the division or payment of the participant's retirement benefits. For example, a qualified domestic relations order could provide that the former spouse is not entitled to any survivor benefits under the Plan."

S. Rep. No. 575, 98th Cong., 2d Sess 16 (Aug. 6, 1984).

Similarly, the helpful examples provided by yourself during the final House debate on the Retirement Equity Act specifically indicated how portions of the participant's accrued benefit would be converted into payments to a divorced

spouse and a surviving spouse in this situation. See 130 Cong. Rec. H8761-62 (Aug. 9, 1984).

Although it was clearly contemplated that a plan would not have to pay the same benefit to both the divorced spouse and the surviving spouse, there is no explicit "carve out" in the survivor benefit rules for benefits previously assigned under a QDRO. Moreover, in the case of an exempt profit-sharing or stock bonus plan that generally provides 100 percent of the account balance to the surviving spouse in the event of death, there is no specific statutory provision that benefits need not be paid to the surviving spouse to the extent previously assigned to an alternate payee under a QDRO. In this regard, we are very concerned that courts might interpret the foregoing legislative history as applying only to those plans which are generally subject to the joint and survivor rules, and not to individual account plans which are exempt from such rules pursuant to Code section 401(a)(11)(B)(iii).

We believe these extremely important issues merit statutory confirmation. Otherwise, surviving spouses may assert that they have a statutory right to unreduced benefits, and plans will be in danger of having to make double payments.

3. Where an Alternate Payee Chooses To Receive Benefits While the Participant Continues Working and Is Not Fully Vested, It Should Be Confirmed That the Plan is Not Required To Increase Benefits to the Alternate Payee To Reflect Subsequent Vesting

In some cases a participant will not be fully vested upon reaching a plan's earliest retirement age (within the meaning of Code section 414(p)(4)(B)). A divorced spouse may nevertheless wish to receive benefits beginning at that date, rather than wait until the participant may become fully vested, and a QDRO may provide for such earlier receipt of benefits.

Section 414(p)(4)(A)(ii) indicates that, where the alternate payee chooses to receive benefits before the participant terminates plan participation, the alternate payee's entitlement is based on the benefits accrued as of the date on which payment is to begin under the QDRO. We request confirmation that, in such cases, the plan is not required to provide increased or additional benefits to the alternate payee whenever the participant's vesting percentage increases. This is consistent with the initial report of the Senate Finance Committee on the Retirement Equity Act:

The special rule provides that in the case of a participant who has attained the earliest retirement age applicable to the participant under a plan, an order will not fail to be a qualified order merely because it requires a plan to pay benefits to an alternate payee in an amount determined as if the participant had retired at that time. Accordingly, the benefit payable to the alternate payee would not reflect subsequent benefit accruals or vesting by the participant.

S. Rep. No. 285, 98th Cong., 1st Sess. 19 (Oct. 29, 1983). To our knowledge, this vesting issue is not specifically addressed in subsequent reports or explanations.

A related issue is whether, in this same situation where the divorced spouse receives benefits and the participant continues working, the divorced spouse is entitled to share in any early retirement subsidy. The compromise reached on this second issue was that the divorced spouse would not be entitled to the subsidy unless the participant subsequently retires to qualify for the subsidy and the QDRO provides for increased payments to the divorced spouse in that event. See S. Rep. No. 575, 98th Cong., 2d Sess. 21 (Aug. 6, 1984). The apparent purpose of this compromise was to minimize "game playing" by participants at the expense of the divorced spouse. It was believed that a participant might otherwise delay retirement until the divorced spouse began to receive payments, so that the full value of any subsidy might be retained by the participant.

This opportunity for "game playing" does not exist in the vesting area, because the expected increase in the vesting percentage each year will be readily apparent and the divorced spouse can determine whether to wait for possible further vesting or receive immediate payments. In addition, the administrative burdens placed on plans if recalculation and increased benefits were required would frequently be substantial. Many plans provide for graduated vesting over a period of years, and recalculation could thus be required 5 or even 10 times in the case of some QDROs. One way to clarify this point would be to revise the parenthetical language contained in section 414(p)(4)(A)(ii) to read as follows (new matter underlined):

(but taking into account only the present value of the benefits which were actually accrued and nonforfeitable as of such date and not taking into account the present value of any employer subsidy for early retirement)

4. The Federal Income and Gift Tax Consequences
of Spousal Waivers of Benefits Should Be Clarified

A spouse may consent to waive post-retirement survivor benefits, preretirement survivor benefits, and the right to receive 100 percent of the account balance in an exempt profit-sharing or stock bonus plan. An area of considerable confusion is in what situations, if any, are benefits nevertheless taxable to the spouse under assignment of

income principles? One argument is that, because benefits payable under qualified plans are only taxed when actually paid to the recipient, spouses should not be taxed on death benefits that they consent to forego in favor of another beneficiary. In any event, if spouses are to be taxed on death benefits they consent to waive, this important consequence should be clearly understood by spouses.

A similar problem arises in the gift tax area. Because consent is irrevocable by the spouse, it could be argued that a gift takes place at the time the consent is given. In this regard, we note that section 152(e)(2)(A) of H.R. 1800 would repeal section 2517 of the Code, which currently eliminates up to half of the potential gift tax liability, at least in community property states. Also, it appears that spousal consent of payment to a designated beneficiary would not constitute a "qualified disclaimer" under Code section 2518 and thus the exception provided by that section would be unavailable.

Section 2(f)(1) of H.R. 2110 contains a special transition rule for certain spousal waivers made on or before the close of first plan year to which the Act applies. The proposed statutory language states that such waivers would not result in gift tax, and the May 14, 1985 explanation of the bill by the Joint Committee staff indicates that such waivers would not increase a spouse's income. These pro-

visions imply that waivers outside of this very limited transition period generally will have income and gift tax consequences to consenting spouses. If intended, these important results should be explicitly stated and clarified. For example, does the "gift" take place when the waiver is signed or when the benefit is paid?

5. The Proposed Amendments to the Spousal Consent Rules Should Be Clarified

Section 2(b)(6) of H.R. 2110 would amend the spousal consent rules to provide that consent is only effective where (1) the spouse "designates a beneficiary" which may not be changed without spousal consent, or (2) the consent specifically permits designations of beneficiaries by the participant without any requirement of further consent by the spouse.

We have several comments on these provisions. First, the proposed language could be interpreted to require the election to designate a beneficiary in all cases if the spousal consent is to be effective. Assume, however, a defined benefit plan where the spouse's consent to an election out of the preretirement or post-retirement survivor coverage results in the participant's receipt of larger annuity benefits and no death benefits payable to any other person. In order to deal with this common situation, proposed section 417(a)(2)(A)(ii) could

be revised to include the following underlined language at the beginning thereof: "if the plan provides for designation of another beneficiary where such election is made, such election designates a beneficiary which may not be changed without spousal consent"

Second, the "designates a beneficiary" concept raises a variety of questions in terms of exactly how specific the designation must be, the effects of subsequent events, etc. For example, we would appreciate clarification in the committee report of how the following situations would be resolved.

1. Spouse consents to payment to "my child" or "my children" at the time when the spouse and participant have one child. A second child is born. Does either of the above consents permit division of the benefits among the two children, or is a new consent required?
2. Spouse consents to payment of equal shares to two children. May the participant subsequently designate that 60 percent of the benefits will be paid to the first child and 40 percent to the second? What if the spouse had consented to payment to "my children" without further elaboration?
3. Spouse consents to payment to a trust. May the participant redirect payments to a second trust? What if the beneficial ownership of the two trusts is identical?
4. May the spousal consent limit the form of payment to the other beneficiary? For example, suppose the spouse specifies that the beneficiary will receive payments in the form of a life annuity. May the participant direct that benefits be paid to this same beneficiary in a lump sum?

Finally, we support the provision of the bill which would allow the spouse to provide a one-time consent to beneficiary designations which may be made or changed in the future. In this regard, we disagree with the Treasury Department position that such "blanket consent" would seriously erode the original policy of the rules. We would expect that there will be a number of cases where (because of precise personal financial circumstances) spouses are willing to forego any direct interest in the participant's benefits and will not want to be bothered with having to provide additional consents as the participant changes beneficiaries. We also believe that, with relatively few exceptions, most individuals will understand the distinction between consenting to a specific beneficiary and providing a blanket consent. Accordingly, we recommend that this type of flexibility for plan participants and their spouses be preserved.

6. The Transition Rule To Avoid Double Death Benefits Should Be Revised Or Eliminated, To Remove Any Implication that Double Benefits Are Required Outside the Scope of the Rule

Section 2(f)(1) of H.R. 2110 provides that, in the case of a plan participant who dies before the expanded survivor annuity rules apply to the plan in general, but whose

surviving spouse is nevertheless entitled to benefits because of the special rule of section 303(c)(2) of the Retirement Equity Act, the amount of any death benefit payable to any beneficiary may be reduced by the amount required to be provided to the surviving spouse. We understand that this provision was intended to help plans by making it clear that the same benefits do not have to be paid twice, i.e., to both the designated beneficiary and the surviving spouse.

Unfortunately, this provision leaves the strong negative implication that plans may be required to pay the same benefit twice where a participant dies after the survivor benefit rules are generally applicable to the plan. For example, take the case of a calendar year single employer plan, for which the expanded survivor benefit rules became effective January 1, 1985. Many such plans have not yet been amended to incorporate the new requirements, and thus the terms of the plan may currently provide for payment to a nonspouse beneficiary. Such plans are not required to be amended to reflect the new rules until the end of 1985 (retroactive, of course, to the beginning of 1985). Section 2(f)(1) of H.R. 2110 leaves the strong implication that, where a participant in such a plan dies in 1985 before the plan is amended, double payment of the same benefit is

required. While we assume that such a result was not intended, we are very concerned that courts might interpret the provision to require double payments.

We suggest that this transition rule should be broad and not be limited to participants who die before the survivor benefit rules apply to the plan. Another possible approach is to delete section 2(f)(1) and address this important issue in the committee report. Thus, for example, the legislative history could make it clear that the general intent of Congress was that survivor benefits which were mandated by section 401(a)(11) and section 417 (including the transition rules) are to be offset against benefits payable to other beneficiaries so that plans would only have to pay the same benefits once.

In addition, it should be made clear that, merely because the election period ends with the participant's death, a surviving spouse may still voluntarily disclaim any interest in the participant's benefits (e.g., for estate tax purposes) after the participant's death as long as the applicable rules are followed (subject to such income, estate, and gift tax consequences as may attach to such disclaimer). In this regard, we see no reason why plans should be forced to pay benefits directly to surviving spouses who make proper disclaimers in favor of another person.

7. The Tax Consequences of QDRO Payments To Alternate Payees Other Than Former Spouses Should Be Clarified

Section 2(c)(1) of H.R. 2110 would amend Code section 402(a)(9), which relates to the tax treatment of an alternate payee receiving benefits under a QDRO. We understand that the intent of the amendment is generally to tax the participant on a QDRO payment if not made to a spouse or former spouse. For example, we understand that QDRO payments to a child would be taxed to the parent participant.

Although the apparent intent of this change is to minimize tax planning opportunities to divorcing spouses (and to prevent indirect deductions of child support payments), it does raise a number of important questions. We request that the related tax consequences of this amendment be clarified. In particular:

1. If a QDRO payment is made to a child, should information reporting on Form 1099R (or Form W-2P) be made as if the payment were made to the parent participant? We assume that such reporting would be appropriate.
2. Do the pension withholding rules under Code section 3405 apply to QDRO payments to a child, and, if so, how? For example, who should receive notice or elect out? Because of the lack of symmetry between the recipient of benefits and the payor of tax, we suggest that such payments be totally exempt from withholding.

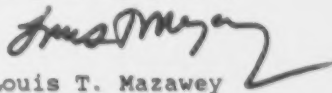
3. May the child roll over QDRO payments to an IRA pursuant to Code section 402(a)(6)(F)? If so, is the parent's tax liability reduced? We assume that the child would be taxed on subsequent IRA distributions.
4. Does Code section 402(e)(4)(M) continue to apply to permit possible lump sum treatment with respect to other benefits taxed to (and in this case actually paid to) the parent participant?

We would emphasize that these are real issues of immediate concern to participants and plans. For example, Chevron would like to amend its section 402(f) notices to benefit recipients to provide guidance with respect to issues 3 and 4 above. Clarification of these issues, either in the statute or in the committee report, would be extremely helpful.

* * *

We appreciate this opportunity to comment. We would be pleased to discuss any of the above matters further with you or your staff.

Very truly yours,



Louis T. Mazawey



Douglas W. Ell



THE
ERISA
INDUSTRY
COMMITTEE

June 5, 1985

The Honorable William L. Clay
Chairman
Subcommittee on Labor-Management
Relations
Committee on Education & Labor
2451 Rayburn House Office Building
U.S. House of Representatives
Washington, D.C. 20515

Attention: Phyllis Borzi

Dear Mr. Chairman:

Enclosed please find five copies of a statement by The ERISA Industry Committee in response to your request for comments on H.R. 2110, a bill making technical corrections to the Retirement Equity Act of 1984 (P.L. 98-397). (See Subcommittee press release dated May 16, 1985). The statement includes both comments on the text of the technical corrections bill and additional suggestions the Committee may wish to add to this bill when it is considered in committee mark-up.

Thank you for your consideration of these matters.

Sincerely,

A handwritten signature in dark ink, appearing to read "Mark J. Ugoretz", written over a horizontal line.

Mark J. Ugoretz
Executive Director

MJU/je
Enclosures



THE
ERISA
INDUSTRY
COMMITTEE

May 28, 1985

STATEMENT OF THE
ERISA INDUSTRY COMMITTEE
REGARDING H.R. 2110, AMENDING
THE RETIREMENT EQUITY ACT OF 1984,
SUBMITTED TO THE COMMITTEE
ON EDUCATION AND LABOR
OF THE U.S. HOUSE OF REPRESENTATIVES

The ERISA Industry Committee ("ERIC") is a non-profit association of over one hundred major corporations doing business in a wide variety of American industries. ERIC's members maintain pension and welfare plans for millions of participants and beneficiaries. ERIC's views are representative of a broad cross-section of major plan sponsors in the private employee benefits community.

Recommended Changes

ERIC recommends that the following changes be made in H.R. 2110:

§ 2(a)(1). To correct clerical errors, "are" should be changed to "is" on line 16, page 2, and line 25, page 3; a closing parenthesis should be added on line 19, page 2, immediately after "consecutive"; and the period should be change to a comma on line 11, page 4.

§ 2(a)(2). Section 2(a)(2) amends I.R.C. § 402(e) to provide that in determining whether a distribution that becomes payable on account of separation from service is a lump sum distribution, the balance to the credit of the employee will be determined without regard to any increase in vesting that may occur if the employee is re-employed by the employer; if the employee elects ten-year averaging with respect to the distribution and is later reemployed by the employer and his vested interest in his previously accrued benefits thereby increases, the tax benefits derived by the employee from his election of ten-year averaging are to be recaptured, and the prior election of ten-year averaging is to be disregarded in determining whether the employee may later elect ten-year averaging. The recapture approach would unduly complicate an already complex provision and should be deleted. The problem that the recapture approach addresses is adequately taken care of by the "look-back" rule of § 402(e)(2) and the only-one-election-after-age-59-½ rule of § 402(e)(4)(B). However, if the recapture provision is retained, it should be revised to make it clear that the

prior lump sum distribution shall not be taken into account under the "look-back" rule. Since the benefits of ten-year averaging with respect to the prior distribution would already have been recaptured, it would be inappropriate to include the prior distribution in the look-back calculation.

§ 2(b)(2)(A)(ii) & (B)(ii). Section 2(b)(2)(A)(ii) & (B)(ii) amends the transferee plan rules of the Code and ERISA to provide that if separate accounts are maintained for the transferred assets "and any income therefrom," the transferee plan rules apply only to the transferred assets, and not to the other plan assets pertaining to the participant for whom the transfer was made. The amendment should be revised to replace "any income therefrom" with "any income allocable thereto" to avoid any suggestion that the transferred assets must be invested separately; the bill should require separate accounting, not separate investment. In addition, if it is intended to apply the transferee plan rules to both the transferred assets and the income allocable thereto, the amendment should also be revised to state that the rules will "apply only with respect to the transferred assets, adjusted to reflect any gains or losses allocable thereto" (new language underscored).

§ 2(b)(4). Section 2(b)(4) amends the survivor annuity provisions of the Code and ERISA to require a plan to provide that no portion of a participant's accrued benefit may be used as security for a loan without the consent of the participant's spouse. The terms of the amendment indicate that the spousal consent requirement will not apply to a plan (e.g., a profit-sharing or stock bonus plan) that is exempt from the survivor annuity provisions by reason of I.R.C. § 401(a)(11)(B)(iii) & (C) and ERISA § 205(b)(1)(C) & (2). This is so because exempt plans are not subject to the provisions of I.R.C. § 417 and ERISA § 205 in which the loan provisions will appear. However, to eliminate any possible misunderstanding, the Committee's report should state explicitly that exempt plans are not subject to the loan provisions. (Any other result would make no sense, since a participant may make a withdrawal from an exempt plan without obtaining spousal consent.)

The amendments should also be revised to make it clear (i) when spousal consent must be given (presumably, when the security interest is given -- which is not necessarily at the same time that the loan is made), (ii) that, once given, a spouse's consent may not be revoked, and (iii)

that a consent given by one spouse is binding on a subsequent spouse.

To correct a clerical error, "subsection (c) (1) (C)" should be changed to "subsection (a) (1) (C)" on line 6, page 11.

Section 2(b)(4) applies to loans made after April 18, 1985. This early effective date (the date on which H.R. 2110 was introduced) is unreasonable and should be postponed. Plan administrators cannot reasonably be expected to be able to comply with the new spousal consent provisions imposed by § 2(b)(4) as early as April 19, 1985. The effective date should give plan administrators a sufficient amount of time, after the bill is enacted, to learn about the new provision, to understand it, and to change their administrative procedures to comply with it. Accordingly, § 2(b)(4) should become effective no earlier than six months after the date of enactment of H.R. 2110.

§ 2(b)(5). Section 2(b)(5) amends I.R.C. § 417(a)(3)(B) and ERISA § 205(c)(3)(B) to extend the period for providing an explanation of the preretirement survivor annuity in the case of a participant who is hired after the close of the plan year preceding the plan year in which he attains age 35. In order to clarify its meaning, the amendment should be revised as follows: "in which the participant attains age 35, or, if the participant is hired after the close of the plan year preceding the plan year in which the participant attains age 35 (or within less than a reasonable period before such date), within a reasonable period after the participant is hired" (new language underscored).

§ 2(b)(6). Section 2(b)(6) amends the spousal consent requirements that govern an election to waive a survivor annuity by providing that either (i) the participant's election must designate a beneficiary that may not be changed without the spouse's consent or (ii) the consent of the spouse must permit the participant to designate beneficiaries without any requirement of further spousal consent. The amendment fails to address the common situation in which the participant's election involves no beneficiary at all -- for example, where the participant elects a single life annuity in lieu of a qualified joint and survivor annuity or where the participant declines the qualified preretirement survivor annuity and foregoes any preretirement death benefit under the plan. The amendment also does not specify whether, after the spouse has consented to the participant's

election, the participant may change the form of the plan benefit without being required to obtain further spousal consent. These flaws could be remedied by revising the amendment to read, in part, as follows: "Such election designates a benefit option and, if applicable, a beneficiary, neither of which may be changed without spousal consent (unless the consent of the spouse permits changes in the benefit option, beneficiary, or both by the participant without any requirement of further consent by the spouse)".

The amendment should also provide that a plan may require either that all spousal consents must be restricted (i.e., limited to the particular benefit option and beneficiary (if any) elected) or that all spousal consents must be unrestricted (i.e., permitting subsequent changes without further consent by the spouse). This rule should be effective as of August 23, 1984. (If, contrary to our recommendation, a more restrictive rule is adopted, the new, more restrictive rule should apply only to consents given at least six months after the enactment of H.R. 2110.)

§ 2(c)(1). Section 2(c)(1) provides that where distributions are made to an alternate payee under a qualified domestic relations order, the distributions shall be included in the gross income of the alternate payee only where the alternate payee is the participant's spouse or former spouse; otherwise the distributions are included in the participant's gross income. This provision makes a substantive, nontechnical change in the law, and should be deleted. The REA made clear that the alternate payee is to be charged with receipt of the distributions made pursuant to a qualified order, regardless of whether the alternate payee is the participant's spouse. The proposed change makes a substantive change in this rule, and it will now be difficult to explain to participants why they are being taxed on income that they do not receive. Because the current law is easy to explain and to administer, it should not be changed. In any event, if the law is changed, conforming changes should be made in I.R.C. § 72(m)(10) (which requires the allocation of the participant's after-tax contributions among all alternate payees) and I.R.C. § 402(a)(1) (which requires plan distributions to be charged to the "distributee").

§ 2(c)(2)(i). To correct two clerical errors, line 5 on page 16 of the bill should be revised to read: "order determined to be qualified domestic".

§ 2(c)(2)(iv). To correct a clerical error, "beginning" should replace "beginnig" on line 9 of page 17. In addition, in order to make the amendment more accurate, "on" should be deleted and replaced with "as of" in line 9 on page 17; the same change should be made in line 19 on page 18.

§ 2(c)(4)(A)(v). Section 2(c)(4)(A)(v) amends I.R.C. § 414(p) to provide that the fact that a plan makes a payment to an alternate payee will not cause the plan to fail to meet the requirements of I.R.C. § 401(a) & (k) prohibiting payment of benefits before termination of employment. The amendment further provides that the foregoing protection against a court-ordered violation of § 401(a) or (k) will not apply if the present value of the payments to the alternate payee exceeds \$3,500.

This provision should refer to I.R.C. § 409(d) as well as to § 401(a) & (k). See S. Rep. No. 575, 98th Cong., 2d Sess. 21 (1984).

The \$3,500 limitation is wholly inappropriate and should be deleted. REA's qualified domestic relations order provisions clearly contemplate that a qualified order may require the payment of benefits before the participant has terminated employment. There is no justification for disqualifying a plan merely because it has observed the terms of a qualified domestic relations order.

The Joint Committee staff's description of H.R. 2110 indicates that this provision is intended to apply to a distribution that is made before the participant has either separated from service or attained the earliest retirement age under the plan. Section 2(c)(4)(A)(v) makes no reference to the plan's earliest retirement age and thus does not accomplish what the staff believes to have been intended. If the bill is revised to reflect this intention, corresponding changes should be made in the definition of a qualified order in I.R.C. § 414(p)(4) and ERISA § 206(d)(3)(E), which delineate the extent to which a qualified order may require payments not provided for under the plan. If these changes are not made, an order that requires a payment before the plan's earliest retirement age will not be a qualified order.

ERIC supports the Treasury Department's recommendation regarding § 2(c)(4)(A)(v): the provision should state that a plan may make payments to an alternate payee before the participant either separates from service or

attains the plan's earliest retirement age if (i) a qualified order directs that the payments be made and (ii) the plan itself authorizes the payments.

§ 2(d). To correct a clerical error, "'qualifying rollover distribution'" should replace "'qualified rollover distribution'" in § 2(d)(1). A conforming change should be made in the heading of I.R.C. § 6652(j) by replacing "Certain Qualifying Rollover Distributions" with "Eligible Rollover Distributions."

§ 2(f)(1). Section 2(f)(1) amends REA § 303(c) to provide that in the case of a participant who is covered by a qualified preretirement survivor annuity pursuant to the transition rule set forth in REA § 303(c)(2), "the amount of any death benefit" payable to any beneficiary shall be reduced by "the amount payable to the surviving spouse" by reason of § 303(c)(2). In the interest of accuracy, the references in this provision to "the amount" of certain benefits should be changed to "the present value" of those benefits.

As drafted, the amendment requires a plan to offset the survivor annuity against the other death benefit. There is no apparent reason why a plan should be compelled to make this reduction. It should be sufficient to give each plan the option to make the reduction and to make it clear that a plan will not be disqualified under I.R.C. § 401(a) if it exercises this option.

In addition, the wording of the amendment suggests that a preretirement survivor annuity will be paid pursuant to REA § 303(c)(2). In fact, the annuity will be paid pursuant to plan provisions that comply with § 303(c)(2). The amendment should be revised to reflect this fact.

Finally, § 2(f)(1) should be expanded to include any participant described in REA § 303(c)(2)(A) & (B) who (i) is a participant in a plan that is amended, during the first plan year to which the REA amendments apply, to exempt it from the survivor annuity provisions, and (ii) dies on or after the date of enactment of REA and on or before the date the plan amendment is adopted.

Recommended Additions

ERIC recommends that the following provisions be added to H.R. 2110:

Anticutback Rule

(I.R.C. § 411(d)(6); ERISA § 204(q))

1. The bill should make clear that an alternative form of payment that is available only in the discretion of the plan administrator or a plan fiduciary is not an "optional form of benefit" for purposes of the anticutback rule. Likewise, the bill should make clear that the exercise of discretion under such a provision is not an amendment of the plan for purposes of the anticutback rule.

2. The bill should make clear that a plan amendment that eliminates the subsidy under a subsidized qualified preretirement survivor annuity does not reduce the participant's accrued benefit for purposes of the anticutback rule.

3. The bill should make clear that the anticutback rule does not prevent a plan from being amended to reduce benefits to reflect the cost of providing the qualified preretirement survivor annuity.

Maternity/Paternity Leave

(I.R.C. §§ 410(a)(5), 411(a)(6);
ERISA §§ 202(b)(5), 203(b)(3))

1. The bill should make it clear that a plan that uses the elapsed time method (and which therefore already credits service for any absence of up to one year) is not required to credit additional service pursuant to REA's maternity/paternity leave provisions.

Qualified Survivor Annuities

(I.R.C. §§ 401(a)(11), 417; ERISA § 205)

1. The bill should amend the exception for profit-sharing and stock bonus plans to permit such plans to impose a one-year-of-marriage requirement without losing their eligibility for the exception. The bill should also make clear that I.R.C. § 401(a)(11)(B)(iii)(II) and ERISA § 205(b)(1)(C)(ii) do not require such plans to allow participants to elect life annuities.

2. The bill should clarify three aspects of the special rule regarding the qualified preretirement survivor annuity for a defined contribution plan in I.R.C. § 417(c)(2) and ERISA § 205(e)(2). First, the bill should make clear that the value of the participant's account balance may be adjusted for investment gains and losses occurring between the participant's date of death and the valuation date used to determine the amount of the annuity. Second, the bill should clarify when the survivor annuity must begin. Third, the bill should make clear that only the vested portion of the participant's account balance is taken into account under the special rule.

3. The bill should clarify the definition of "annuity starting date" in I.R.C. § 417(f)(2) and ERISA § 205(h)(2) by referring to "termination of employment" as well as to "retirement" and "disability."

4. The bill should make clear that a plan may presume that every participant is married, and may charge for the cost of preretirement survivor annuity protection, until and unless the participant waives the coverage in advance.

5. The bill should provide that when a participant files an effective waiver of qualified preretirement survivor annuity coverage, the plan may rely on the waiver until notified in writing that the participant has remarried.

6. The bill should make clear whether an election to waive the qualified joint and survivor annuity before the beginning of the applicable election period is valid. This is not made clear by I.R.C. § 417(a)(1)(A) and ERISA § 205(c)(1)(A).

7. The bill should make clear that since the qualified preretirement survivor annuity rules applied before the generally applicable effective date of REA, a plan may pass on the cost of the preretirement survivor annuity coverage during the pre-effective-date period automatically to all participants.

8. In many countries, the position of "notary public" does not exist. The bill should provide that in the case of a spousal consent executed outside of the United States, the consent may be witnessed by the equivalent of a notary public in the country where the consent is executed (as well as by a plan representative).

9. The bill should clarify that a plan may require a preretirement survivor annuity to begin as of the month next following the participant's death (or, if later, as of the month in which the participant would have attained the earliest retirement age under the plan).

10. The bill should correct a technical error in I.R.C. § 417(c)(1)(B) and ERISA § 205(e)(1)(B) by providing that if the participant dies after the earliest retirement date under the plan, the earliest period for which the surviving spouse may receive a payment under the qualified preretirement survivor annuity is the month following the month of the participant's death.

11. The bill should make clear that, in determining the size of the payments under a qualified joint and survivor annuity or a qualified preretirement survivor annuity, a plan may presume that the spouse's age is identical to that of the employee and may place the burden on the employee to prove otherwise.

12. The bill should amend REA § 303(e)(4)(A)(ii) to provide that a plan will not be deemed to fail to give notice before the Treasury fulfills its obligation to provide guidance on how to give notice under § 303(e)(4)(A)(i).

Qualified Domestic Relations Orders

(I.R.C. §§ 401(a)(13), 414(p); ERISA § 206(d))

1. The bill should make clear that a plan is bound by a qualified domestic relations order only if the plan has been made a party to the litigation and the court has jurisdiction over the plan.

2. The bill should amend I.R.C. § 414(p)(7)(C) and ERISA § 206(d)(3)(H)(iii) to make clear that a plan administrator may, in its discretion, refrain from paying the segregated amounts until the expiration of the 18-month period, even if it is determined that the order is not a qualified domestic relations order. This would confirm that the plan administrator has the authority to suspend payment, in its discretion, if it has reason to believe that the order may be amended within the 18-month period to cure any defect that originally prevented the order from qualifying.

Cash-Outs

(I.R.C. § 411(a)(11)(A); ERISA § 203(e)(1))

1. The bill should clarify that the bar against the immediate mandatory distribution of the present value of a benefit that exceeds \$3,500 does not apply to a defined contribution plan.

2. The bill should clarify that the bar against the immediate mandatory distribution of the present value of a benefit that exceeds \$3,500 applies only to lump sum distributions and not to annuity or installment distributions.

3. The bill should clarify that accumulated deductible employee contributions are disregarded when applying the \$3,500 limit.

Notice of Forfeitability of Benefits

(I.R.C. § 6057; ERISA § 105)

1. The bill should clarify whether the required notice that benefits are forfeitable must be included in the statement of total accrued benefits and nonforfeitable accrued benefits furnished to plan participants who have not separated from service. Cf. H.R. Rep. No. 655, 98th Cong., 2d Sess. (Part 2) 3, 23 (1984); S. Rep. No. 575, supra, at 24-25.

GIBSON, DUNN & CRUTCHER
LAWYERS333 SOUTH GRAND AVENUE
LOS ANGELES CALIFORNIA 90071

(213) 228-7000

TELEX 874W30 GIBTRASK LSK

CABLE ADDRESS GIBTRASK LOS ANGELES CA

June 4, 1985

WASHINGTON
1050 CONNECTICUT AVENUE N.W.
WASHINGTON D.C. 20036
(202) 855-8500DENVER
1801 CALIFORNIA STREET
DENVER CO. 80202
(303) 228-7000DALLAS
1000 PACIFIC AVENUE
DALLAS TEXAS 75201
(214) 879-8100CENTURY CITY
2028 CENTURY PARK EAST
LOS ANGELES CALIFORNIA 90067
(213) 552-8500NEWPORT CENTER
800 NEWPORT CENTER DRIVE
NEWPORT BEACH CALIFORNIA 92660
(714) 759-1800SAN DIEGO
600 B STREET
SAN DIEGO CALIFORNIA 92101
(619) 231-1000SAN JOSE
ONE A WATER BUILDING
SAN JOSE CALIFORNIA 95113
(415) 389-2000JAN A. GIBSON 842 1872
W. E. DUNN 866 805
ALBERT CRUTCHER 860 181NEW YORK
8 WEST 87TH STREET
NEW YORK NEW YORK 10018
(212) 608-7800EUROPE
104 AVENUE RAYMOND PONDARE
75016 PARIS FRANCE
801 8185
CABLE ADDRESS GIBTRASK PARIS
TELEX 81008 GIBTRASK FLONDON
78 SOUTH AUDLEY STREET
LONDON W1Y 8TF ENGLAND
CABLE ADDRESS GIBTRASK LONDON W
TELEX 2773 GIBTRASK G
AFFILIATED SAUDI ARABIA OFFICEMEXICO PLAZA
AIRPORT ROAD
P.O. BOX 5026
MEXICO SAUDI ARABIA
ATTN: 10883
TELEX EUROPA PANAMA S.

WRITERS DIRECT DIAL NUMBER

(213) 229-7654

OUR FILE NUMBER

C64230-0000-1

Ms. Phyllis Borzi
2451 Rayburn House Office Building
Washington, D.C. 20515Re: H.R. 2110

Dear Ms. Borzi:

This is to submit for consideration a proposed technical correction to the Retirement Equity Act of 1984 (the "Act") to be included in H.R. 2110. We are suggesting this technical correction to clarify the provisions of the Act relating to the payment of joint and survivor annuities under a money purchase plan, as required by Act Section 203, which amended Section 401(a)(11) of the Internal Revenue Code (the "Code") and added Code Section 417.

One of our clients has asked us to submit this proposal for your consideration. This client, which has approximately 55,000 employees, sponsors a money-purchase thrift plan. The individuals responsible for administering the plan are concerned by the implications of the differing interpretations of the provisions of the Act relating to the timing of participant elections to waive the automatic joint and survivor annuity upon separation from service prior to disability or some stated retirement age. It is our client's view that the Act should be clarified to permit a participant to make the election to waive the

payment of benefits in the form of the joint and survivor annuity at any time following separation from service for any reason.

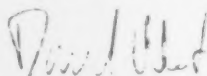
Reason for Change. Sections 103 and 203 of the Act require a defined contribution plan which is subject to the minimum funding standards under Code Section 412 to provide payment of benefits with a value of more than \$3500 in the form of a qualified joint and survivor annuity, unless an election to waive the qualified joint and survivor annuity is made by the participant, with the consent of the participant's spouse during the prescribed election period. That prescribed election period starts 90 days before the "annuity starting date," which is the date as of which retirement or disability benefits are paid under the plan. It might be argued (although we disagree with such interpretation) that a participant who separates from service more than 90 days before the earliest retirement age under the plan cannot make a valid election to waive the joint and survivor annuity form at the time of that separation (unless the separation is due to "disability").

Most money purchase plans distribute vested account balances to participants upon separation from service and do not defer payment until the participant reaches retirement age, as in the case of defined benefit plans. In the case of a money purchase thrift-savings plan in existence prior to the Act, plan participants generally made contributions to the plan with the reasonable expectation that they would be paid their account balance upon separation from service, without regard to retirement or disability. If a participant now separating from service prior to retirement or disability cannot make a valid election until 90 days before retirement or disability, participants will be denied a right which they reasonably have relied on having--the right of withdrawal of their own funds. Any such "cutback" is not only fundamentally unfair, but seems to be inconsistent with the Congressional policy reflected in Code Section 411(d)(6), as amended by Act Section 301(a)(1) to prohibit the elimination of optional forms of benefits.

Proposed Change. We propose the modification of the definition of the "applicable election period" in Code Section 417(a)(5)(A) to permit a participant who separates from service under a money purchase plan prior to retirement or disability to make the required election to waive distribution of his accrued benefit in the form of qualified joint and survivor annuity, as follows:

- (A) in the case of an election to waive the qualified joint and survivor annuity form of benefit,
 - (i) in the case of a defined benefit plan, the 90-day period ending on the annuity starting date, or
 - (ii) in the case of a defined contribution plan, the period which begins 60 days prior to the date on which occurs the separation from service and ends on the earlier of the date distribution of the vested accrued benefit is made or commences to be made under the plan, or the annuity starting date.

Very truly yours,



David West

DW:ls

cc: Sarah Manning
William Kilberg
S. David Blinn
Peter C. Turza
Carol B. Bierhorst

Statement of the
Investment Company Institute on
the Retirement Equity Act of 1984
Technical Corrections Act (H.R. 2110)
before the
House Committee on Education and Labor
Subcommittee on Labor-Management Relations

The Investment Company Institute* (the "Institute") offers the following comments and proposals regarding H.R. 2110, a bill making technical corrections to the Retirement Equity Act of 1984.

The Requirement to Purchase a Commercial Annuity

It has recently come to the Institute's attention that the Internal Revenue Service ("IRS") may be interpreting the joint and survivor and preretirement survivor annuity requirements of Code sections 401(a)(11) and 417, as amended by the Retirement Equity Act, in a manner that would require that certain defined contribution retirement plans provide for the purchase of commercial annuity. The Institute believes that such an interpretation is not justified under either the specific language or intent of the Retirement Equity Act and that statutory or Committee Report language clarifying this point are highly desirable.

As revised by the Retirement Equity Act, section 401(a)(11) of the Code requires that certain defined contributions

*The Investment Company Institute is the national association of the American mutual fund industry. Its membership includes 1,261 open-end investment companies ("mutual funds"), their investment advisers and principal underwriters. Its mutual fund members have assets of about \$378.1 billion, accounting for approximately 90% of total industry assets, and have over 20 million shareholders.

plans* provide benefits in the form of a "qualified joint and Survivor annuity" and also provide death benefits in the form of a "qualified preretirement survivor annuity". Both of these forms of benefits are described in Code section 417.

Section 417(b) of the Code defines a "qualified joint and survivor annuity" as:

"... an annuity -

(1) for the life of the participant with a survivor annuity for the life of the spouse which is not less than 50 percent of (and is not greater than 100 percent of) the amount of the annuity which is payable during the joint lives of the participant and spouse, and

(2) which is the actuarial equivalent of a single annuity for the life of the participant.

Such term also includes any annuity in a form having the effect of an annuity described in the preceding sentence."[emphasis added]

Section 417(c)(2) of the Code defines a "qualified preretirement survivor annuity" for a defined contribution plan as, "an annuity for the life of the surviving spouse the

*This requirement extends to essentially all defined contribution retirement plans other than those profit-sharing plans which automatically provide for the participant's accrued, vested benefit to be paid to his or her surviving spouse in the event of death.

actuarial equivalent of which is no less than 50 percent of the account balance of the participant as of the date of death."

Prior to the revision of the joint and survivor rules by the Retirement Equity Act of 1984, most defined contribution plans satisfied the joint and survivor rules without having to offer the purchase of an annuity contract. This was accomplished by paying out the participant's account balance upon death after the participant attained early retirement age.

Although we recognize that the recent changes to the joint and survivor rules reflect an intent to require defined contribution pension plans to provide greater protection for participants' spouses than was previously required, we believe that this protection can be accomplished without the purchase of a commercial annuity contract from an insurance company. Moreover, we believe that statutory language cited above, specifically permits plans to provide the required joint and survivor protection through means that would not contravene a participant's chosen investment medium.

The Institute's Proposal

In light of a recent IRS interpretation of these joint and survivor and preretirement survivor annuity requirements,* the Institute recommends that the Retirement Equity Act be

*IRS LRMs (model language) issued for use in master and prototype plans have required that certain defined contribution plans provide for the purchase of a commercial annuity to satisfy the joint and survivor and preretirement survivor annuity definitions.

statutory or Committee Report language providing that an annuity from a defined contribution plan will be considered a "qualified joint and survivor annuity" if it meets the following requirement:

- o the payment in any year does not exceed the the value of the account balance at the beginning of that year divided by the joint and last survivor life expectancy of the participant and spouse, based on the ages of those individuals at the beginning of that year.

Similarly, we propose that the Retirement Equity Act be revised to clearly indicate that an annuity from a defined contribution plan will be considered a "qualified preretirement survivor annuity" if it meets the following requirements:

- o at least 50 percent of the participant's account balance at death is used to provide an annuity to the spouse; and
- o the payment in any year does not exceed the the remaining death benefit at the beginning of that year divided by the spouse's life expectancy, based on the spouse's age at the beginning of the year.

The joint and survivor rules were enacted to provide extra protection to the spouses of plan participants in their retirement years. This assurance of retirement income can be adequately provided under our proposal, without the purchase of a commercial annuity contract.

Attached hereto as Appendix A are three exhibits which we believe demonstrate the adequacy of the survivor's benefits that

would be provided under the Institute's proposal. Tables 1, 2, and 3 show the annual distribution that would be made under our proposal to a participant who retires at age 65 with a spouse who is five years younger. The tables assume a fund with an annual return of 3 percent, 5 percent, and 7 percent, respectively.* Note that, regardless of the funds' earnings, the payments continue at a significant level for many years. Assuming a 5 percent fund annual return, the annual payment will not drop under 50 percent of the initial payment until the spouse has attained age 102. Furthermore, the payment in year 36 exceeds the amount paid in the first year.

Reviewing these projections, we believe that our proposal is consistent with the policy objective of providing significant protection for participants' spouses. Similar patterns would result in the case of the preretirement survivor annuity. In that case, however, there should even be less concern, because the spouse will not be "sharing" the distribution with any other beneficiaries.

In addition, an interpretation of the provisions of the Retirement Equity Act which would require that plans provide for the purchase of a commercial annuity represents a governmental

*From 1979 to the present, the average annual return on money market funds has ranged between a low of 8.58 percent and a high of 16.82 percent. (From Donoghue's Money Fund Report.) For the past ten years common stock mutual funds have performed at an average annual rate of about 15 percent, and for the past twenty-five years common stock funds have performed at an average annual rate of about 9.2 percent.

intrusion into the marketplace which would have an unfair competitive effect on the mutual fund industry. If certain defined contribution plans invested in mutual funds are required to offer benefits in the form of an insurance company annuity contract, significant amounts will have to be withdrawn from mutual funds for the purchase of annuity contracts. Plan participants would be denied the opportunity to fund their retirement plan through their preferred investment medium.

For these reasons, the Institute urges the adoption of the proposal set forth above to clarify the joint and survivor and preretirement survivor annuity requirements of the Retirement Equity Act.

* * * *

The Institute appreciates the opportunity to present these comments to the Subcommittee. Please contact us if you have any questions regarding these proposals.

TABLES 1, 2, AND 3

- o Projects annual payments from a fund based on Institute proposals
- o Assumptions:
 - Payments commence when male participant retires at age 65 with female spouse, age 60.
 - One payment each year at beginning of year.
 - Joint and last survivor life expectancies based on Table II of 1.72-9 as adjusted for annual payments in accordance with 1.72-5(a)(2).
 - Fund with an annual rate of return at 3 percent, 5 percent, or 7 percent annually.

MINIMUM DISTRIBUTIONS FOR LUMP SUM PRESENT VALUES

INTEREST RATE: 7.00%

MALE AGE (x)	FEMALE AGE (x)	PRESENT VALUE	J & S LIFE EXPECTANCY	ANNUAL PAYMENT	PV AFTER DISTRIBUTION
65	60	\$102,000	25.1	\$3,984	\$96,216
66	61	\$103,737	24.3	\$4,220	\$98,529
67	62	\$105,405	23.5	\$4,465	\$102,930
68	63	\$107,984	22.7	\$4,757	\$103,227
69	64	\$110,453	22.0	\$5,021	\$105,432
70	65	\$112,812	21.2	\$5,321	\$107,491
71	66	\$115,015	20.5	\$5,611	\$109,425
72	67	\$117,063	19.7	\$5,942	\$111,121
73	68	\$118,899	19.0	\$6,258	\$112,642
74	69	\$120,527	18.3	\$6,586	\$113,942
75	70	\$121,916	17.6	\$6,927	\$114,959
76	71	\$123,038	16.9	\$7,290	\$115,756
77	72	\$123,861	16.3	\$7,599	\$116,262
78	73	\$124,401	15.6	\$7,974	\$116,426
79	74	\$124,576	15.0	\$8,305	\$116,271
80	75	\$124,410	14.4	\$8,640	\$115,770
81	76	\$123,874	13.6	\$9,108	\$114,765
82	77	\$122,799	13.2	\$9,323	\$113,495
83	78	\$121,441	12.6	\$9,638	\$111,823
84	79	\$119,629	12.1	\$9,887	\$109,743
85	80	\$117,425	11.5	\$10,211	\$107,214
86	81	\$114,719	11.0	\$10,429	\$104,292
87	82	\$111,590	10.5	\$10,628	\$102,952
88	83	\$108,030	10.0	\$10,803	\$97,227
89	84	\$104,033	9.6	\$10,837	\$93,196
90	85	\$99,722	9.1	\$10,958	\$88,761
91	86	\$94,975	8.7	\$10,917	\$84,058
92	87	\$89,942	8.3	\$10,836	\$79,106
93	88	\$84,643	7.9	\$10,714	\$73,929
94	89	\$79,104	7.5	\$10,547	\$68,557
95	90	\$73,356	7.2	\$10,188	\$63,167
96	91	\$67,589	6.9	\$9,796	\$57,794
97	92	\$61,839	6.6	\$9,370	\$52,472
98	93	\$56,142	6.3	\$8,911	\$47,231
99	94	\$50,537	6.0	\$8,423	\$42,114
100	95	\$45,062	5.7	\$7,906	\$37,157
101	96	\$39,758	5.4	\$7,363	\$32,395
102	97	\$34,663	5.1	\$6,797	\$27,866
103	98	\$29,817	4.8	\$6,212	\$23,605
104	99	\$25,257	4.5	\$5,613	\$19,645
105	100	\$21,020	4.2	\$5,005	\$16,015
106	101	\$17,136	3.9	\$4,394	\$12,742
107	102	\$13,634	3.6	\$3,787	\$9,847
108	103	\$10,536	3.3	\$3,193	\$7,343
109	104	\$7,857	3.0	\$2,619	\$5,238
110	105	\$5,605	2.7	\$2,076	\$3,529
111	106	\$3,776	2.4	\$1,573	\$2,203
112	107	\$2,357	2.1	\$1,122	\$1,235

MINIMUM DISTRIBUTIONS FOR LUMP SUM PRESENT VALUES

INTEREST RATE:

5.00%

MALE AGE (x)	FEMALE AGE (x)	PRESENT VALUE	J & S LIFE EXPECTANCY	ANNUAL PAYMENT	PV AFTER DISTRIBUTION
65	60	\$102,000	25.1	\$3,984	\$96,016
66	61	\$102,817	24.3	\$4,149	\$90,668
67	62	\$101,521	23.5	\$4,319	\$87,182
68	63	\$102,041	22.7	\$4,495	\$87,546
69	64	\$102,423	22.0	\$4,656	\$87,768
70	65	\$102,650	21.2	\$4,842	\$87,814
71	66	\$102,704	20.5	\$5,010	\$87,695
72	67	\$102,579	19.7	\$5,207	\$87,372
73	68	\$102,241	19.0	\$5,381	\$86,862
74	69	\$101,703	18.3	\$5,558	\$86,145
75	70	\$102,952	17.6	\$5,736	\$85,216
76	71	\$99,977	16.9	\$5,916	\$84,061
77	72	\$98,765	16.3	\$6,059	\$82,705
78	73	\$97,341	15.6	\$6,240	\$81,101
79	74	\$95,656	15.0	\$6,377	\$80,278
80	75	\$93,743	14.4	\$6,510	\$87,233
81	76	\$91,595	13.6	\$6,735	\$84,860
82	77	\$89,103	13.2	\$6,750	\$82,352
83	78	\$86,472	12.6	\$6,863	\$79,607
84	79	\$83,588	12.1	\$6,908	\$76,660
85	80	\$80,514	11.5	\$7,021	\$73,512
86	81	\$77,186	11.0	\$7,017	\$70,171
87	82	\$73,679	10.5	\$7,017	\$66,662
88	83	\$69,996	10.0	\$7,000	\$62,990
89	84	\$66,146	9.6	\$6,890	\$59,256
90	85	\$62,218	9.1	\$6,837	\$55,381
91	86	\$58,150	8.7	\$6,684	\$51,466
92	87	\$54,040	8.3	\$6,511	\$47,526
93	88	\$49,925	7.9	\$6,317	\$43,588
94	89	\$45,768	7.5	\$6,102	\$39,665
95	90	\$41,648	7.2	\$5,785	\$35,864
96	91	\$37,657	6.9	\$5,458	\$32,202
97	92	\$33,810	6.6	\$5,123	\$28,687
98	93	\$30,121	6.3	\$4,781	\$25,340
99	94	\$26,607	6.0	\$4,435	\$22,173
100	95	\$23,281	5.7	\$4,084	\$19,197
101	96	\$20,157	5.4	\$3,733	\$16,424
102	97	\$17,245	5.1	\$3,381	\$13,864
103	98	\$14,557	4.8	\$3,033	\$11,524
104	99	\$12,100	4.5	\$2,689	\$9,411
105	100	\$9,882	4.2	\$2,353	\$7,529
106	101	\$7,906	3.9	\$2,027	\$5,879
107	102	\$6,172	3.6	\$1,715	\$4,458
108	103	\$4,681	3.3	\$1,418	\$3,262
109	104	\$3,425	3.0	\$1,142	\$2,284
110	105	\$2,398	2.7	\$888	\$1,510
111	106	\$1,585	2.4	\$661	\$925
112	107	\$971	2.1	\$462	\$509

MINIMUM DISTRIBUTIONS FOR LUMP SUM PRESENT VALUES

INTEREST RATE:

3.02%

MALE AGE (x)	FEMALE AGE (x)	PRESENT VALUE	J & S LIFE EXPECTANCY	ANNUAL PAYMENT	PV AFTER DISTRIBUTION
65	62	\$122,020	25.1	\$3,984	\$20,216
66	61	\$98,896	24.3	\$4,070	\$24,627
67	62	\$97,671	23.5	\$4,156	\$23,515
68	63	\$96,321	22.7	\$4,243	\$12,277
69	64	\$94,842	22.0	\$4,311	\$22,529
70	65	\$93,245	21.2	\$4,398	\$20,846
71	66	\$91,512	20.5	\$4,464	\$27,249
72	67	\$89,659	19.7	\$4,551	\$25,129
73	68	\$87,661	19.0	\$4,614	\$22,247
74	69	\$85,539	18.3	\$4,674	\$20,665
75	70	\$83,291	17.6	\$4,732	\$28,552
76	71	\$80,915	16.9	\$4,788	\$22,127
77	72	\$78,411	16.3	\$4,812	\$22,622
78	73	\$75,802	15.6	\$4,862	\$22,943
79	74	\$73,277	15.0	\$4,872	\$22,222
80	75	\$70,252	14.4	\$4,879	\$22,373
81	76	\$67,334	13.6	\$4,951	\$22,322
82	77	\$64,255	13.2	\$4,888	\$22,357
83	78	\$61,169	12.6	\$4,855	\$22,314
84	79	\$58,023	12.1	\$4,794	\$22,212
85	80	\$54,826	11.5	\$4,760	\$22,242
86	81	\$51,541	11.0	\$4,685	\$22,650
87	82	\$48,262	10.5	\$4,596	\$22,665
88	83	\$44,975	10.0	\$4,498	\$22,478
89	84	\$41,692	9.6	\$4,343	\$22,343
90	85	\$38,470	9.1	\$4,227	\$22,242
91	86	\$35,269	8.7	\$4,054	\$22,215
92	87	\$32,152	8.3	\$3,874	\$22,278
93	88	\$29,126	7.9	\$3,687	\$22,442
94	89	\$26,223	7.5	\$3,494	\$22,729
95	90	\$23,392	7.2	\$3,249	\$22,142
96	91	\$20,746	6.9	\$3,027	\$22,732
97	92	\$18,271	6.6	\$2,768	\$22,523
98	93	\$15,968	6.3	\$2,535	\$22,434
99	94	\$13,837	6.0	\$2,326	\$22,532
100	95	\$11,876	5.7	\$2,084	\$22,793
101	96	\$10,087	5.4	\$1,868	\$22,219
102	97	\$8,465	5.1	\$1,660	\$22,825
103	98	\$7,010	4.8	\$1,460	\$22,549
104	99	\$5,716	4.5	\$1,270	\$22,446
105	100	\$4,579	4.2	\$1,090	\$22,489
106	101	\$3,593	3.9	\$921	\$22,672
107	102	\$2,752	3.6	\$764	\$22,988
108	103	\$2,047	3.3	\$620	\$22,427
109	104	\$1,470	3.0	\$492	\$22,822
110	105	\$1,029	2.7	\$374	\$22,635
111	106	\$654	2.4	\$273	\$22,382
112	107	\$393	2.1	\$187	\$22,206

ARNOLD & PORTER

CABLE "ARYDPO"
TELEPHONE (202) 872-6700
TELEX 89 2733

1200 NEW HAMPSHIRE AVENUE, N.W.
WASHINGTON, D. C. 20036

1700 LINCOLN STREET
DENVER, COLORADO 80203
(303) 863-1000

(202) 872-6700

K. PETER SCHMIDT
DIRECT LINE 202 872 6834

May 23, 1985

Committee on Education and Labor
Subcommittee on Labor-Management Relations
U.S. House of Representatives
2451 Rayburn House Office Building
Washington, D.C. 20515

Attention: Phyllis Borzi, Pension Counsel

Re: Comments on H.R. 2110, Making
Technical Corrections to the
Retirement Equity Act of 1984

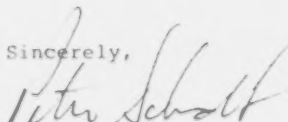
Dear Ms. Borzi:

Pursuant to your notice of May 16, 1985, I enclose five copies of the comments of the National Coordinating Committee for Multiemployer Plans,*/ on H.R. 2110, proposing technical corrections to the Retirement Equity Act of 1984. This document was originally prepared and submitted in connection with House Ways and Means Committee Hearings on both H.R. 1800, the Technical Corrections Act of 1985, and H.R. 2110. It therefore includes comments on both bills. Comments on H.R. 2110 begin at page 21.

If you have any questions, or if we can be of any further help or assistance, please call me or my associate Vivian H. Berzinski (872-8610).

Best regards.

Sincerely,



K. Peter Schmidt

Enclosures

*/ The NCCMP is a non-profit, tax-exempt organization established after Congress enacted ERISA in 1974. It consists of representatives of more than 140 pension and welfare plans, or their sponsors, through which, in the aggregate, the interests of approximately three million persons are represented. On behalf of its affiliated multiemployer plans and their participants and beneficiaries, the NCCMP is entirely engaged in monitoring the development -- legislative, administrative, and judicial -- of the laws relating to the structuring and administration of multiemployer pension and welfare plans.

**National Coordinating Committee for
Multiemployer Plans**

SUITE 603 • 815 SIXTEENTH STREET, N.W., WASHINGTON, D.C. 20006 • (202) 347-1461

COMMENTS OF THE
NATIONAL COORDINATING COMMITTEE
FOR MULTIEMPLOYER PLANS
ON H.R. 1800,
THE TECHNICAL CORRECTIONS ACT OF 1985,
AND H.R. 2110, MAKING TECHNICAL
CORRECTIONS TO THE RETIREMENT EQUITY ACT OF 1984

OUTLINE

OF COMMENTS ON H.R. 1800,
THE TECHNICAL CORRECTIONS ACT OF 1985,
AND H.R. 2100, MAKING TECHNICAL CORRECTIONS TO
THE RETIREMENT EQUITY ACT OF 1984

- A. The Technical Corrections Act of 1985 (H.R. 1800) ("Bill").
1. Permissible welfare plan reserves.
 - a. The limits for tax deductible contributions and tax exempt reserves for collectively bargained welfare funds should be set forth explicitly in Code¹ section 419A.
 - b. Additional welfare plan reserve limit issues.
 - i. The welfare benefit plan reserve limit transition rules of Code section 419A(f)(7) should be made available to all plans that had reserves as of the beginning and end of the plan year that includes the date the DRA was enacted. Further, it should apply to collectively bargained plans that had reserves as of the end of such plan year and either: (1) did not increase contribution rates between enactment of the DRA and the end of such plan year; or (2) did increase such rates, but did not at that time plan to decrease them after the end of such plan year. The transition rules of Code section 512(a)(3)(E) should apply to reserves as of the end of such plan year.
 - ii. The Bill should make clear that the exemption of an insurance policy from the definition of "fund" applies even if an experience-rated refund or insurance policy dividend is payable

¹ Internal Revenue Code of 1954, as amended.

to a collectively bargained trust,
and is not taxable to the trust.

2. Other multiemployer plan issues.

- a. The collective bargaining exceptions to the nondiscrimination requirements of Code sections 419A(e)(1) and 4976(b)(1) should apply in all cases where welfare benefits in the aggregate are bargained to be provided in accordance with section 302(c)(5) of the Taft-Hartley Act.
- b. The current collectively bargained plan effective date for the rules added by the DRA to the Unrelated Business Taxable Income ("UBTI") provisions of Code section 512, and the excise tax provisions of Code section 4976 should not be changed.
- c. Multiemployer plans should not be required to be aggregated with other plans of contributing employers for any purposes of Code section 419A. Workable rules should be promulgated whereby contributing employers can permissively aggregate their single employer plans with their allocable portions of the multiemployer plans to which they contribute.
- d. The Bill or its legislative history should clarify whether the proposed repeal of Code section 2517 (which exempts from gift tax an employee's designation of a beneficiary under a qualified plan) would subject a contingent or revocable designation of a plan beneficiary to tax. It should also clarify whether a spouse that consents to waive his or her right to a death benefit would be subject to gift tax liability, and how any gift or estate tax of qualified plan death benefits is coordinated with the income tax treatment of plan payments to the beneficiary.
- e. Multiemployer plans should be exempted from the top-heavy plan provisions of Code sections 416 and 401(a)(10)(B). Workable rules should be provided whereby employers, in testing their single employer plans for top-heaviness,

can receive credit for their "share" of benefits under a multiemployer plan to which they contribute. Such credit should be available regardless of whether benefits under the plans are "comparable."

- f. Code section 419(e)(2), which defines "welfare benefits" should explicitly include in such definition a post-retirement cost of living adjustment benefit, which, pursuant to ERISA section 3(2)(B), is treated as a welfare benefit under Department of Labor regulations.

B. H.R. 2110 ("Bill"), Making Technical Corrections to the Retirement Equity Act of 1984 ("REA").

1. A spouse that waives his or her right to death benefits should not be given a power of approval of his or her successor beneficiary. Certain technical problems also exist with respect to the Bill's proposal to require such approval.
2. The amendments proposed to section 303(c) of REA to avoid requiring that plans pay duplicate death benefits as a result of REA's pre-retirement spousal death benefit rules should allow plans to pay both a pre-existing death benefit and the REA benefit if their sponsors wish to do so. Further, the time period for the proposed opportunity for a spouse to waive his or her benefit should be extended to make such waiver feasible. Tax consequences of such a waiver should also be clarified.
3. Qualified domestic relations orders ("QDROs").
 - a. Under REA, an ex-spouse is entitled to receive benefits under a QDRO even if the employee is still working. The rule that protects the tax-qualified status of a pension plan that honors such an award should not be changed. Providing payment pursuant to a QDRO should not disqualify a plan even if the benefits it must pay to the ex-spouse have a present value of more than \$3,500. Certain technical problems also exist with respect to such proposal.
 - b. REA should be clarified to state that a plan should not be required to comply with

or otherwise modify any actions addressed by a QDRO that take place before the QDRO is delivered to the plan.

4. The requirement of spousal consent to use of a participant's accrued benefit as security for a loan should be made effective January 1, 1986.

COMMENTS ON H.R. 1800, THE TECHNICAL
CORRECTIONS ACT OF 1985 AND
H.R. 2110, MAKING TECHNICAL CORRECTIONS
TO THE RETIREMENT EQUITY ACT OF 1984

The National Coordinating Committee for Multiemployer Plans ("NCCMP") is pleased to offer its comments on H.R. 1800, the Technical Corrections Act of 1985, and H.R. 2100, making technical corrections to the Retirement Equity Act of 1984.

The NCCMP is a nonprofit, tax-exempt organization established after Congress enacted ERISA in 1974. It consists of representatives of more than 140 pension and welfare plans, or their sponsors, through which, in the aggregate, the interests of approximately three million persons are represented. On behalf of its affiliated multiemployer plans and their participants and beneficiaries, the NCCMP is entirely engaged in monitoring the development -- legislative, administrative, and judicial -- of the laws relating to the structuring and administration of multiemployer pension and welfare plans.

We suggest reconsideration of several aspects of the technical corrections bills as they would apply to multiemployer plans. We also note the possibility of technical improvements in certain provisions.

A. The Technical Corrections Act of 1985 ("Bill")

1. Permissible Welfare Plan Reserves

a. Reserve Limits Applicable to Collectively Bargained Welfare Plans

Section 419A² as added by the Deficit Reduction Act of 1984 ("DRA"), provides tax deductible reserve limits for welfare plans. Section 419A(f)(5) directs the Secretary of Treasury to provide special, higher limits for collectively bargained plans no later than July 1, 1985.

The Conference Report states:

"Certain collectively bargained plans. -- By July 1, 1985, the Treasury Department is to publish final regulations establishing special reserve limit principles with respect to welfare benefit funds maintained pursuant to an agreement that the Secretary of Labor finds to be a collective bargaining agreement between employee representatives and one or more employers, if there is evidence of good faith bargaining over the benefits provided by the plan between the employee representatives and the employer (or employers).

In establishing these limits, the Treasury is to presume that reserves in such plans are not excessive because

² Unless otherwise stated, all references herein are to the Internal Revenue Code of 1954, as amended.

of the arm's length negotiations between adversary parties inherent in the collective bargaining process. Because contributions under such plans are often made on the basis of a defined contribution fixed over a multiyear period on the basis of economic assumptions which prove to be incorrect and because such contributions may be the only source of benefits to be provided during layoffs, strikes, lockouts, and economic recession, these special limits are to allow substantial flexibility in determining the application of these provisions with respect to such plans." H.R. Rep. No. 861, 98th Cong., 2d Sess. 1158 (1984).

In this report, Congress clearly stated two things about collectively bargained plans. First, the nature of such plans, and of the collective bargaining process, generally precludes the abuses of principal concern. Second, the practical requirements of such plans (e.g., the need to set contributions at some fixed rate based on hours of work or units of production) and the plans' basic economics,³ mandate special reserve principles.

Recognizing the basic facts set forth above, Congress also gave specific instruction as to how the situation should be handled: the reserves of such plans are to be presumed reasonable. In other words, the reserve limitations of this newly-enacted provision

³ Employer contributions do not rise to meet plan needs. Instead, they generally fall in times of aggravated participant need, e.g., recession, strike or layoff.

are not generally to apply in the case of collectively bargained plans.

Perhaps it is possible for the Treasury to fashion regulations accurately reflecting the Congressional intent discussed above. However, after a review of many specific situations, and a good bit of effort, we have been unable to devise any formula or other standardized approach that would cover the vast array of fact patterns actually presented.

Perhaps the regulations could merely restate the generalized intent reflected in the report, providing that the reserves of collectively bargained plans will be deemed within the applicable reserve limitations, unless the IRS establishes their unreasonableness in particular situations. Such a regulation would be entirely appropriate if the problem is actually to be addressed by regulation. However, the Congressionally imposed deadline is upon us, and guidance is desperately needed now.

Given the foregoing, we submit that Congressional intent would best be served by explicit statutory language setting forth a general rule on the reasonableness of reserves in collectively bargained plans. Such an

approach makes particularly good sense in light of the nearness of the July 1, 1985 deadline set by Congress for final regulations on this subject. Proposed regulations have not yet been issued, and timely issuance of carefully developed regulations seems unlikely given the current agenda of appropriate Treasury and IRS personnel.

Consequently, we suggest that Code section 419A(f)(5) be amended in its entirety to read as follows:

"(5) Higher Limit in Case of
Collectively Bargained Plans --

(A) Notwithstanding any other provisions of this section, for purposes of sections 419 and 512, the limit determined under this section for a qualified asset account established by a welfare benefit fund maintained pursuant to one or more agreements that the Secretary of Labor finds to be collective bargaining agreements between employee representatives and one or more employers shall be no less than the amount credited to that account, if --

(i) there is evidence of good faith bargaining over funding for the benefits provided through the fund and

(ii) the Secretary does not find that the fund's reserves are unreasonable, taking into account past experience and reasonable expectations. For this purpose, the amount in a reserve attributable to employer contributions shall be deemed to be reasonable if the level of contributions required was reasonably

expected to be necessary to maintain the plan of which the fund is a part, under all of the circumstances existing and anticipated at the time the collective bargaining agreement setting the contribution obligation was agreed to.

(B) For purposes of this paragraph, the term "amount credited to that account" includes assets to provide for the future payment of any welfare benefit, within the meaning of section 419(e)(2), in addition to the benefits listed in subsection (a) of this section."

The problems described above are particularly acute with respect to multiemployer plans. Such plans are required by the Taft-Hartley Act to function as jointly administered trusts. In these circumstances benefits cannot be provided directly from the general assets of employers. "Welfare benefit funds" must be utilized if benefits are to be provided at all.

Further, once an employer makes a contribution to a multiemployer plan, the money is gone forever. Also individual employers, as such, typically have little or no direct role in the plan trustees' decisions about what benefits to provide. Thus, unlike the situation that may exist in some single-employer plans, there is neither opportunity nor motive for "packing" with excess funds in order to accelerate deductions.

b. Additional Welfare Plan Reserve
Limit Issues

Additional reserve limit issues are addressed below. We note, however, that these issues will become moot if the amendment suggested above becomes law.

i. Reserve Limit Transition Rules

Section 151(a)(7) of the Bill would make the reserve limit transition rules of section 419A(f)(7) available only to funds that had reserves "as of July 18, 1984." This is clearly meant to deny transition relief to employers who, for tax purposes, made large welfare plan contributions between enactment of the DRA and the end of 1984.

However, the new rule, as presently structured, would create unnecessary administrative burdens. Plans do not keep daily records of the status of their reserves. Thus, most plan trustees will not know if the plan had reserves as of July 18, 1984. They would be able to determine this, if at all, only through retroactive reconstruction of the plan's financial status as of that date.

We suggest that the transition rules be made available, instead, to plans that had reserves as of

both the beginning and the end of the plan year that includes July 18, 1984. This would adequately test plans on the basis of information they ordinarily have available.

In addition, for collectively bargained plans, the transition rules should apply if:

"(A) The plan had reserves as of the end of the plan year that includes July 18, 1984, and

"(B) Either:

"(i) no increase in the rate of contributions under the collective-bargaining agreement was negotiated between July 18, 1984, and the end of the plan year that included July 18, 1984; or

"(ii) If a post-July 18, 1984, contribution rate increase was negotiated, such increase did not provide for a decrease after the end of the plan year that included July 18, 1984."

This would make the transition rules unavailable to plans that increased contributions until the end of 1984 to inflate the 1984 reserve for tax purposes. However, the rules would remain available in bona fide situations where deficits existed at the beginning of the 1984 plan year but, because of benefit cuts or

legitimate contribution rate increases, there were surpluses by the end of that year.

A similar problem arises under section 151(a)(10)(C)(iii) of the Bill. That section would amend Code section 512(a)(3)(E)(iii)(II) to impose income tax on the earnings of post-retirement medical or life insurance welfare fund reserves in excess of the amount the fund had accumulated for such purposes as of July 18, 1984. As stated, it would be difficult, if not impossible, for plans to determine the reserves that existed on such a specific date. Instead, the test should be the existing level of reserves for such purposes as of the end of the plan year that includes July 18, 1984. Safeguards similar to those suggested above with respect to section 419A could be provided to prevent abuse.

ii. Treatment of Certain Insurance Contracts

Section 151(a)(8) of the Bill would exclude certain types of insurance contracts from the definition of a "welfare benefit fund." The exclusion would apply only if "the amount of any experience-rated refund or policy dividend payable to an employer with respect to a policy year is treated by the employer as received

or accrued in the taxable year in which the policy year ends." This limitation is clearly intended to apply the credit income to reduce the employer's deduction for the initial premium. However, this rationale does not apply in the context of tax-exempt trusts. Accordingly, the legislative history should state that this limitation applies only if the experience credit is paid directly to an employer, and is not relevant if the contract holder that receives the credit is a tax-exempt trust.

2. Other Multiemployer Plan Issues

There are a number of other issues which are of importance to multiemployer plans, regardless of the disposition of the collectively bargained reserve limit issue.

a. Collective Bargaining Exceptions to Nondiscrimination Requirements of Sections 419A(e)(1) and 4976(b)(1)

Section 419A(e)(1) currently provides that no reserve may be taken into account under section 419A(c)(2) for post-retirement medical benefits or life insurance benefits unless the plan meets the nondiscrimination requirements of section 505(b)(1). Section 4976 imposes an excise tax on employers maintaining funds that provide

"disqualified benefits." Under section 4976(b)(1), "disqualified benefits" include post-retirement medical or life insurance benefits, unless the plan meets the nondiscrimination requirements of section 505(b)(1) with respect to such benefits.

Sections 151(a)(3) and 151(a)(11) of the Bill would apply these rules to plans, such as collectively bargained plans, that are not otherwise subject to section 505. There would be an exception for benefits provided by a plan maintained under a collective bargaining agreement, if the post-retirement medical and life insurance benefits were the subject of good-faith bargaining.

Post-retirement welfare benefits, as such, are not necessarily the subject of direct bargaining in the multiemployer context. The bargaining parties often denominate separate contributions for pension and for welfare benefits. They ordinarily do not specify the actual benefits to be provided or the portion of the welfare benefit contributions that will be used to provide any particular type of benefit. Instead, these decisions are left to the plan trustees.

Since the intent of the change seems to be to continue the current law standard exception for collectively bargained plans, an additional exemption should be added with respect to both sections 419A(e)(1), and 4976(b)(1) for "benefits provided in the manner described in paragraphs (5) et seq. of 29 U.S.C. section 186(c)" -- i.e., collectively bargained and provided through a jointly managed trust in accordance with Taft-Hartley.

b. Effective Date of Section 512
Unrelated Business Taxable Income
("UBTI") and Section 4976 Excise
Tax Changes

Under section 511(e)(2) of the Deficit Reduction Act of 1984 ("DRA"), the new UBTI provisions of section 512, and excise tax provisions of section 4976 will not apply to collectively bargained plans until the first day of the plan year starting after expiration of the longest-running labor contract in effect on July 1, 1985. Section 151(a)(12) of the Bill would add new paragraphs (6) and (7) to the end of section 511(e) as follows:

"(6) Amendments Related to Tax on Unrelated Business Income -- The amendments made by subsection (b) [UBTI provisions] shall apply with respect to taxable years ending after December 31, 1985. . . .

"(7) Amendments Related to Excise Taxes on Certain Welfare Benefit Plans. -- The amendments made by subsection (c) [excise taxes on disqualified benefits] shall apply to benefits provided after December 31, 1985."

The Bill should make clear that these new paragraphs are not intended to override the collective bargaining effective date provided in paragraph (2) of section 511(e) of the DRA. It would be difficult, if not impossible, for collectively bargained plans to comply with a January 1, 1986 effective date. Treasury will not announce the special reserve limits applicable to such plans until July 1, 1985, at the earliest. Further, there is no practical opportunity to readjust contribution rates until the expiration of the currently effective collective bargaining agreement. Finally, until passage of the Technical Corrections Bill, the extent, if any, to which a plan's benefit structure will have to be amended will remain uncertain. See section 1., supra.

c. Aggregation of Plans

Section 419A provides limits on the amount of disability and SUB or severance pay benefits and life insurance benefits that can be taken into account in

determining permissible plan reserves. Further, it treats amounts allocable to individual accounts of key employees to pay post-retirement medical benefits as annual additions under section 415(c).

Section 151(a)(6) of the Bill would provide that, for purposes of these provisions, all welfare benefits of an employer must be treated as a single fund. For all other purposes of Section 419A, an employer would be permitted to elect to treat two or more welfare benefit funds he maintains as one fund.

Multiemployer welfare plans have no way of knowing whether contributing employers have other welfare plans. They have no control over or knowledge of contributions to or benefits under other plans of contributing employers. Thus, requiring multiemployer plans to aggregate single employer benefits for this purpose would be unfair and unworkable.

Further, higher reserve limits are to be prescribed for collectively bargained plans, including multiemployer plans. Thus, the limits on the amount of disability and SUB or severance pay benefits and life insurance benefits should not apply to such plans. With respect to the section 415(c) limits, if benefits under an

aggregation of plans exceed such limits, Treasury regulations provide that benefits under the single employer, rather than the multiemployer, plan will be reduced. See Treas. Reg. §§ 1.415-8(e), 1.415-9(a)(3).

Accordingly, no purpose would be served by subjecting multiemployer plans to the required aggregation rules. Such plans should therefore be exempted.*

The Bill could nevertheless require a single employer plan to be aggregated with a multiemployer plan to the extent of that portion of the multiemployer plan that is allocable to the employer's employees. If the aggregated plans exceed the limits, however, only the single employer plan should be affected. For this purpose, the Treasury should be directed to promulgate simple, workable rules for allocating a share of the multiemployer plan's assets and liabilities to each contributing employer, without the burden and expense of tracing their actual source.

* We note that aggregation of plans is also required for purposes of the UBTI rules added by the DRA. § 512(a)(3)(E)(iii)(III). Our comments apply equally in this context. However, the Secretary of Treasury is empowered to provide exceptions by regulations. We hope and expect that such regulations will provide the necessary exemption.

d. Gift Tax Changes

Section 152(e) of the Bill would repeal section 2517, which creates a gift tax exemption for an employee's designation of a beneficiary under a qualified pension or profit-sharing plan. The statute or legislative history should clarify whether a contingent or revocable designation of a plan beneficiary would be subject to tax. It should also clarify whether a spouse that consents, in accordance with the Retirement Equity Act of 1984, to waive his or her right to a death benefit would be subject to gift tax liability. Income tax treatment of amounts already considered part of a taxable gift or estate should also be clarified.

e. Top-Heavy Plan Provisions

Section 240 of the Tax Equity and Fiscal Responsibility Act of 1982 added a new section 416 which sets forth special rules for top-heavy plans. In general, a plan is considered top-heavy if the present value of the cumulative accrued benefits or aggregate account balances for certain highly paid officers and owners ("key employees") of the employer exceeds sixty percent of the present value of the cumulative accrued benefits or aggregate account balances of all employees under

the plan. Code § 416(g). We note that section 152(d) of the technical corrections bill would make certain changes in the top-heavy provisions of the law.

The facts are that a multiemployer plan cannot be top-heavy, and that the sanctions applicable to top-heavy plans have no practical relevance in the multiemployer plan context.

The vast majority of multiemployer plan participants are bargaining unit employees who are generally not officers or owners of an employer and therefore not key employees. Further, most multiemployer plans provide non-integrated flat-dollar benefits that are unrelated to compensation. Thus, larger dollar benefit amounts are ordinarily based on longer terms of covered service rather than the higher pay that typically accompanies company ownership or officer status. The few key employees that might be covered by multiemployer plans would therefore have no advantage over non-key employees with respect to benefit accrual. It would therefore be virtually impossible for multiemployer plans to satisfy the definitional top-heaviness test of providing in excess of sixty percent of its benefits to key employees. For this reason, it would be unreasonable to subject multiemployer plans

to the administrative compliance burdens of the top-heavy provisions.

Collectively bargained plans, including multiemployer plans, are already expressly exempted from the major substantive top-heavy requirements, *i.e.*, the section 416(b), (c), and (d) requirements relating to faster vesting, minimum benefits or contributions, and a ceiling on the amount of compensation that may be used to compute benefits. Code § 416(i)(4). However, multiemployer plans are not expressly exempted from the section 416(h)(1) reduction in the section 415(e) dollar limitation on combined contributions to and benefits under defined contribution and defined benefit plans maintained by the same employer.

Such plans are further burdened by the section 401(a)(10)(B) requirement that all plans adopt boilerplate language to take effect if they become top-heavy. Under Treasury regulations, a plan is relieved of this requirement if it covers only employees included in a bargaining-unit and employees of employee representatives. This relief is inadequate and impractical, however, because a multiemployer plan may cover a small number of other employees. For example, union members who have become self-employed may, in

some plans, maintain continuity of coverage. A few plans allow "special class" participation through which a company's salaried employees are covered as long as its union-represented employees participate. Further, the Treasury regulations do not make clear whether the exception would apply to plans that cover employees of the plan itself.

It would be unreasonable to subject multiemployer plans to these burdensome provisions, since no meaningful protection to multiemployer plan participants would be provided and no perceived abuses corrected. We therefore seek a technical correction, which would make clear that multiemployer plans are exempted from the top-heavy requirements, including the burdensome requirement to adopt boilerplate, top-heavy provisions that will almost certainly never become effective. The Secretary could be empowered to promulgate regulations limiting this exemption if necessary to prevent abuses.

The technical correction should also make clear that, for purposes of determining the top-heavy status of an employer's single employer plans, employers are to aggregate their share of the accrued liabilities of any multiemployer plan to which they contribute as though it were a separate plan. If this aggregation

group is top-heavy, only the single employer, and not the multiemployer, plan would be considered top-heavy.

Employers should also be permitted to aggregate their single employer plans with their allocable share of a multiemployer plan's benefits, in testing for top-heaviness in their single employer plans. Such aggregation should be available regardless of whether benefits under the multiemployer plan are "comparable" to benefits under the single employer plans. The Secretary of Treasury should be directed to prescribe a simple, workable formula for determining each employer's "share" of multiemployer plan benefits for this purpose, without actually tracing contributions and benefits.

f. Definition of "Welfare Benefit"

Section 419(e)(2) should be amended to make clear that the term "welfare benefit" includes a post-retirement cost-of-living adjustment benefit which, pursuant to ERISA section 3(2)(B), is treated as a welfare benefit under Department of Labor regulations. This would explicitly subject such benefits to the amendments made by the DRA in sections 419, 419A, and 512.

B. H.R. 2110 ("Bill") Making Technical
Corrections to the Retirement Equity
Act of 1984 ("REA")

1. Spousal Consent to Beneficiary
Designation

REA requires written spousal consent to a waiver of the spouse's right to death benefits. It does not require the spouse to formally consent to the employee's election of an alternative payment form, or choice of another beneficiary. Once the spouse relinquishes his or her right to a death benefit, the employee is free to do whatever he or she wants with it.

Section 2(b)(6) of the Bill would amend section 417(a)(2) to give the spouse greater power to determine the disposition of such benefits. The waiver would be effective only if:

"(A)(i) The spouse of the participant consents in writing to such election, (ii) such election designates a beneficiary which may not be changed without spousal consent (or the consent of the spouse permits designations of beneficiaries by the participant without any requirement of further consent by the spouse), and (iii) the spouse's consent acknowledges the effect of such election and is witnessed by a plan representative or a notary public, ..."

The change would apply to benefit elections made after the Bill's date of enactment.

In our view, the prevention of the occasional abuses at which this change is apparently aimed would not justify the administrative burdens that would be imposed on plans. Plans would be required to adopt yet another round of plan amendments. They would have to reprint appropriate forms, revise summary plan descriptions, mail additional explanations to employees etc. (At a minimum, these facts require a delayed effective date in the proposed change.)

There may be times when an employee designates a beneficiary his or her spouse did not contemplate and would not have approved. However, where the spouse has voluntarily waived his or her right to such benefit, the spouse's financial security will ordinarily not be enhanced through an ability to control the designation of the alternative beneficiary, if the employee can still choose a payout form that cuts out the spouse, e.g., lump sum, etc.

There are also technical problems with the proposed change. It would apparently require a spouse's waiver of his or her death benefit to be accompanied by the

designation of another beneficiary. In most cases, however, a waiver of a qualified joint and survivor annuity at retirement will result in higher monthly annuity payments during the employee's lifetime, with no death benefit payable after the employee's death. And pre-retirement death benefits may be waived entirely, to avoid the charge for it that some plans are imposing. At a minimum, the Bill should accommodate these practices.

Further, qualified plans often provide death benefits in addition to, rather than instead of, the qualified spousal benefit. For example, multiemployer defined contribution plans are required to guarantee a spouse a pre-retirement death benefit based on only half of the employee's account. It would be useful for the legislative history to make clear that any waiver requirements apply only to the qualified joint and survivor and preretirement survivor benefits.

Involving the spouse in the beneficiary designation process could also create gift-tax problems for the spouse, if the proposal, in the Technical Corrections Act of 1985, to repeal Section 2517 is passed. If these provisions of the two technical corrections bills are enacted, the gift tax treatment of the spouse should be clarified.

2. Duplicate Death Benefits

Section 2(f) of the Bill would amend the joint and survivor transition rules in section 303(c) of REA to protect plans from having to pay duplicate death benefits as a result of the immediate effective date of REA's pre-retirement spousal death benefit rules, as follows:

"(4) ELIMINATION OF DOUBLE DEATH BENEFITS. -- (A) IN GENERAL. -- In the case of a participant described in paragraph (2), the amount of any death benefit (other than a qualified preretirement survivor annuity) payable to any beneficiary shall be reduced by the amount payable to the surviving spouse of such participant by reason of paragraph (2).

"(B) SPOUSE MAY WAIVE PROVISIONS OF PARAGRAPH (2). -- In the case of any participant described in paragraph (2), the surviving spouse of such participant may waive the provisions of paragraph (2). Such waiver shall be made on or before the close of the first plan year to which the amendments made by this Act apply. Such a waiver shall not be treated as a transfer of property for purposes of chapter 12 of the Internal Revenue Code of 1954 and shall not be treated as an assignment or alienation for purposes of section 401(a)(13) of the Internal Revenue Code of 1954 or section 206(d) of the Employee Retirement Income Security Act of 1974."

A few technical modifications are required with respect to this proposed change. It would apparently require an offset of the spousal benefit in all cases. However, plans often pay both a pre-existing death benefit and the REA benefit (e.g., in a money purchase plan where the REA benefit is only half of the account, or in cases where there is a separate children's benefit). Further, where the spouse is already the designated beneficiary for the pre-existing death benefit, the plan may offer him or her the choice between that and the REA benefit.

Accordingly, we suggest that the word "shall" in the proposed amendment be changed to "may." This would avoid requiring plans to reduce or eliminate benefits they intend to provide in addition to the REA benefit.

In addition, the proposed change would give a spouse the right to waive his or her benefit in favor of another beneficiary. However, such waiver would have to be exercised "on or before the close of the first plan year to which the amendments made by [REA] apply." The amendments made by REA apply first in the plan year that includes August 23, 1984. For most plans, this is the 1984 calendar year. Thus, the waiver

opportunity will have elapsed before the Bill passes. We suggest extending this waiver opportunity to the end of the plan year in which REA is generally effective, i.e., the first plan year beginning after December 31, 1984 (REA section 302(a)) or, for a collectively bargained plan, the first plan year beginning on or after the earlier of: (1) the expiration of the last collective bargaining agreement relating to the plan; or (2) January 1, 1987 (REA section 302(b)). This is appropriate since the waiver right will only be necessary if the participant died in the period between enactment of REA and its general effective date.

The proposed language also protects waiving spouses from gift taxes and from the anti-alienation provisions of ERISA and the Internal Revenue Code. However, it leaves open the possibility that a spouse waiving his or her REA rights in favor of a designated beneficiary might be subject to income tax on the money as an assignment of income. The statutory language or legislative history should make clear that this is not the case.

The legislative history should also note that a settlement of a disputed claim to benefits is not a waiver and would not entail any adverse tax consequences that might otherwise be associated with a waiver.

3. Qualified Domestic Relations
Orders ("QDROs")

a. Limit on QDRO Pay-Outs

REA allows an ex-spouse to receive benefits, under a QDRO, even if the employee is still working. It enacted a special rule protecting the qualified status of pension and 401(k) plans that pay benefits, under these special circumstances, before the participant terminates employment.

Section 2(c)(4)(A)(v) of the Bill would amend Code section 414(p). It would apparently permit a qualified pension or 401(k) plan to make payments to an ex-spouse while the employee is still working only if the present value of the payment is no more than \$3,500.

We can see no justification for subjecting ex-spouses to such hardship with respect to benefits a court has ordered paid (and which REA may otherwise require). There is no reason why an individual entitled to a reasonable pension from his or her ex-spouse's plan should be forced to wait until that ex-spouse terminates employment. Indeed, in many cases, these benefits will be indispensable to the spouse's continued adequate support.

It is also unclear what benefits would be counted in determining whether the \$3,500 limit is satisfied. The proposed language could be construed to count all of the payments that the ex-spouse is expected to receive before the employee terminates employment. Alternatively, it could be construed to count the total payments to which the ex-spouse is entitled.

We note that some plans have already started paying ex-spouses under QDROs without regard to the \$3,500 limit. Thus, additional problems will be created because the proposed effective date of the change is January 1, 1985, the effective date of REA's QDRO provisions.

b. Service of QDROs

The Bill should also include a provision stating that a QDRO (or a non-qualified order) cannot affect any actions taken by a plan before a copy of it is delivered to the plan. For example, a plan that has not received a copy of a QDRO should be permitted to rely on a spousal sign-off, even if the QDRO gives the prior spouse a right to death benefits. It is obviously unfair and unworkable to require a plan to comply with a QDRO it has not received.

4. Spousal Consent To Use Plan Assets
as Security for Loans

Section 2(b)(4) of the Bill would require spousal consent to the use of a participant's accrued benefit as security for a loan. This requirement would be effective for loans made after April 18, 1985.

April 18, 1985 has already passed, and plans have since been making loans without obtaining such spousal consent. Further, after REA and the DRA, plan managers have a great many other amendments to adopt, forms to revise, and other demands on their time. Accordingly, plans should be given a reasonable period prior to effectiveness of this requirement to enable them to make necessary preparations. We suggest January 1, 1986 as a reasonable effective date.



NATIONAL RURAL ELECTRIC COOPERATIVE ASSOCIATION

1800 Massachusetts Avenue, N.W. Washington, D.C. 20036/202-857-9500

STATEMENT OF THE NATIONAL RURAL ELECTRIC COOPERATIVE ASSOCIATION RELATING TO HR 2110, MAKING TECHNICAL CORRECTIONS TO THE RETIREMENT EQUITY ACT OF 1984, BEFORE THE SUBCOMMITTEE ON LABOR-MANAGEMENT RELATIONS

MAY 22, 1985

Mr. Chairman and members of the Subcommittee, my name is Martin D. Wood. I am the Director of the Retirement, Safety and Insurance Department of the National Rural Electric Cooperative Association (NRECA) and the Administrator of the various welfare and pension programs sponsored by NRECA and its members. NRECA is the national service organization of the approximately 1,000 rural electric systems operating in 46 states. These systems bring central station electric service to approximately 25 million farm and rural individuals in 2,600 of our nation's 3,100 counties. Our various programs provide pension and welfare benefits to over 110,000 employees and their dependents in those localities.

The purpose of my comments to you today is to bring to your attention a technical issue concerning a proposal for improving the methods allowed for calculating the Pension Benefit Guaranty Corporation (PBGC) interest rate for lump sum payments, which you may wish to include in HR 2110.

INTEREST RATE ASSUMPTIONS LUMP SUM PENSION DISTRIBUTIONS

The Retirement Equity Act of 1984 (REACT) requires that the interest rate assumption used in calculating the present value of a pension benefit distributed in a lump sum not be

greater than the interest rate used (on the date of distribution) by the Pension Benefit Guaranty Corporation (PBGC) for valuing lump sum distributions on plan terminations. REACT section 205(a). The committee reports state that a plan may provide that the PBGC interest rate in effect on the first day of the plan year be used throughout the plan year. S. Rep. No. 575, 98th Cong., 2d Sess. 24 (1984).

Providing a PBGC referenced interest rate assumption is a salutary change that significantly protects plan participants from unfair or arbitrary interest rate assumptions in valuing lump sum distributions. We feel, however, that the rules provided in REACT are not flexible enough to accommodate the needs of some pension plans in the orderly administration of their pension benefits. To illustrate some of these concerns we will use as an example the multiple employer, master defined benefit pension plan sponsored by the National Rural Electric Cooperative Association (the "NRECA pension plan").

Before the passage of REACT, the NRECA pension plan had provided for the use of the PBGC rate for the calculation of lump sum payments to plan participants. However, the specific method used by the NRECA pension plan does not conform to the REACT specifications in several regards. The NRECA pension plan provides for one PBGC rate to be in effect for the 12 month period from April 1 of one year to March 30 of the next year. The rate to be used for that period is the average PBGC rate in effect over a 12 month period ending June 30. Thus an average PBGC rate is calculated and then becomes effective nine months later. While the method used by the NRECA pension plan varies from REACT in three ways, each difference is occasioned by significant concerns for the orderly administration of the NRECA pension plan.

1. Average Rates. While REACT made no provision for average rates, we feel that a 12 month average is a fairer reflection of the trend of interest rates. It provides over the entire participant population a fairer distribution of lump sum values than a PBGC rate in effect during one month of the year.

2. Spans Two Years. Since in our experience the great majority of retirements occur on December or January, a change of rate at the beginning of a plan year introduces a great variation in lump sum values among retirees. We are

also greatly concerned with the administrative difficulty of changing the lump sum calculation in the middle of the most active retirement period.

3. Nine Month Lag. Potential retirees need stable retirement projections and time to plan for their retirement. We, therefore, allowed a period of nine months from the calculation of the interest rate until it became effective to allow for participant planning before their retirement actually occurs.

While we agree with the need to specify PBGC interest rates for lump sum calculations, we fear that there is not sufficient flexibility provided in REACT to enable the IRS to approve pension plans that may, for good administrative reasons, have variations on the REACT specified method. We therefore suggest that the committee reports accompanying HR 2110, Making Technical Corrections to the Retirement Equity Act of 1984, provide that the Commissioner may issue favorable determination letters to plans providing for PBGC rates in calculating lump sum amounts by methods the Commissioner finds reasonable under the circumstances. The circumstances to be considered should include the orderly administration of the plans, predictability of the lump sum amounts and consistency among the plan participants. For example, an average PBGC rate or one covering a twelve month period spanning two plan years could be permitted by the Commissioner.

This concludes my comments on our proposal to allow additional flexibility in the calculation of the PBGC interest rate for lump sum distributions. I remain willing to respond to any questions the Subcommittee may have on this or any other issue.

In the United States House of Representatives
Committee on Labor and Education
Subcommittee on Labor-Management Relations

Comments on H.R. 2110

Submitted by: John C. Brooks
North Carolina Commissioner of Labor

Date: June 5, 1985

H.R. 2110 proposes technical corrections to the Retirement Equity Act of 1984, including amendments to the Employee Retirement Income Security Act of 1974 (ERISA). While I have no specific comments on the amendments which are proposed, I do wish to urge adoption of a further amendment to ERISA to clarify the interrelationship between ERISA and those state laws whose purposes are to enforce payment of promised wages and wage-related benefits.

A majority of states, including North Carolina, have laws requiring and enforcing the payment of wages promised by employers. Generally, these state wage payment laws apply to wages in the form of payroll benefits such as vacation pay, sick pay, severance pay, or holiday pay.

When Congress enacted ERISA to regulate employee benefit plans, employee welfare benefits were defined in ERISA as including many of the same benefits covered by the state wage payment laws. ERISA, by its own terms, supersedes 'any and all state laws insofar as they may now or hereafter relate to any employee benefit plan.' See § 514(a) of ERISA, 29 U.S.C. § 1144(a).

Because of ERISA's preemption provision, a growing number of employers in various states throughout the nation are challenging, through court and administrative proceedings, the viability of state wage payment laws, making it increasingly difficult for state labor law administrators to enforce those laws. In several cases, courts have ruled that ERISA preempts state laws enforcing such benefits as vacation pay and severance pay. The result of these decisions has been that employees in those states have become less well protected by law when seeking to recover promised wage benefits. Not only do employees lose the assistance of state administrative agencies in collecting their pay, but increasingly courts are applying a less strict standard of liability against employers under ERISA than had been applied under state laws. It is clear from the expression of legislative intent that ERISA was intended to increase protection of employees with respect to their benefits. Insofar as the courts' broad interpretation of ERISA's preemption is creating the opposite result, an amendment to ERISA is appropriate to reverse the effects of these decisions and restore Congressional intent.

Another distressing result of these court decisions is that they upset the traditional division between state and federal jurisdiction. Enforcement of promised wages, like enforcement of other contracts, has long been exercised by

the states under the police powers retained by them under the Tenth Amendment. The ERISA preemption decisions are part of a judicial trend, highlighted by the Supreme Court Decision in *Garcia vs. San Antonio Metropolitan Transit Authority*, to completely erode state's rights under the Tenth Amendment. Apparently, it is left to Congress to reverse that trend.

At its annual convention in Tulsa, Oklahoma, during the week of July 8, 1984, the National Association of Governmental Labor Officials, of which I am a member, adopted a resolution proposing the following amendment to ERISA:

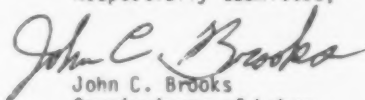
An act to amend and clarify ERISA by adding a second and third sentence to section 514(a), 29 U.S.C. §1144(a):

State laws prohibiting employers from discriminating in the provision of employee benefits, obligating employers to pay promised employee welfare benefits to its employees, and providing for the enforcement of such obligations shall not be considered laws relating to an employee benefit plan. The foregoing sentence shall not apply to employee pension benefit plans.

A copy of that Resolution is attached to my comments as Exhibit A. Also attached and incorporated in these comments by reference are the following items which further explain the nature of the problem which I am requesting you to address: Statement of Interest of Amicus Curiae, Exhibit B, and Argument (pages 8 through 17), Exhibit C, from the Brief of Amicus Curiae State of New York in the case of *Slack and Brooks vs. Burlington Industries, Inc.*, case numbers 84-2241(L) and 84-2257, United States Court of Appeals for the Fourth Circuit; relevant excerpts from the North Carolina Wage and Hour Act, Exhibit D; narrative description of North Carolina Department of Labor, Wage and Hour Division enforcement procedures, Exhibit E; narrative description of the New York Wage and Benefit Payment Statute and enforcement procedures, Exhibit F; Summary Description of Wage Payment Laws of Alaska, Connecticut, District of Columbia, Hawaii, Illinois, Maryland, Montana, Oklahoma, Vermont and Wisconsin, Exhibit G; decisions of four federal district courts ruling on the issue of ERISA preemption of state wage payment laws in Illinois, New York, California, and North Carolina, Exhibits H, I, J, and K.

I respectfully request this subcommittee to study the need to clarify ERISA on the subject of preemption of state wage payment laws and to propose for adoption by Congress the amendment suggested by the National Association of Governmental Labor Officials. If I or my staff can be of any assistance in your consideration of this matter, please do not hesitate to contact me.

Respectfully submitted,



John C. Brooks
Commissioner of Labor
214 West Jones Street
Raleigh, North Carolina 27603
919/733-7166

NAGLO RESOLUTION

ERISA AMENDMENT

Submitted by John C. Brooks
Commissioner of Labor, State of North Carolina

WHEREAS, the majority of states have laws requiring and enforcing the payment of wages promised by employers; and

WHEREAS, the majority of state wage payment laws apply to wages in the form of one or more of the following employee benefits, to wit, vacation holiday pay, sick pay, severance pay or other similar benefits promised by employers; and

WHEREAS, the United States Congress has enacted the Employee Retirement Income Security Act of 1974 (ERISA) which regulates, among other things, employee welfare benefit plans; and

WHEREAS, an employee welfare benefit is defined in ERISA as including many of the same benefits covered by state wage payment laws, to wit, vacation pay, holiday pay, sick pay, severance pay and other similar benefits; and

WHEREAS, ERISA by its own terms supersedes "any and all state laws insofar as they may now or hereafter relate to any employee benefit plan;" and

WHEREAS, the United States Supreme Court has held in the case of Shaw v. Delta Airlines, Inc., _____ U. S. _____, 103 S. CT. 2890 (1983) that "Congress used the words 'relate to' . . . in their broadest sense" and that a law "relates to" an employee benefit plan "if it has a connection with or reference to such a plan;" and

WHEREAS, the United States District Court for the Central District of California has held in the case of California Hospital Association v. Henning, 569 F. Sup. 1544 (C.D. Calif. 1983) California's wage payment law "relates to" employee vacation benefits within the meaning of ERISA and, thus, is superseded by ERISA and is unenforceable; and

WHEREAS, a growing number of employers in various states throughout the nation are challenging through court and administrative proceedings the viability of state wage payment laws in light of ERISA's preemption provision, making it increasingly difficult for state labor law administrators to enforce their states' wage payment laws; and

WHEREAS, pending resolution of the preemption issue by the Supreme Court, administration of state wage payment laws will be greatly hindered, resulting in a substantial reduction in states' abilities to enforce the payment of wages promised to employees; and

WHEREAS, the present controversy over preemption of state wage payment laws by ERISA has resulted and will continue to result in a lessening of protection for employees which was neither intended nor envisioned by Congress; and

WHEREAS, preemption of state wage payment laws by ERISA takes away from the states an area of regulation traditionally reserved to the states and, thus, upsets the traditional balance between state and federal enforcement of wages; and

WHEREAS, states are uniquely qualified and able vis-a-vis the federal government to enforce wage payments and, thus protect their working citizens;

NOW THEREFORE BE IT RESOLVED BY THE NATIONAL ASSOCIATION OF GOVERNMENTAL LABOR OFFICIALS IN ITS 67TH ANNUAL CONVENTION ASSEMBLED IN TULSA, OKLAHOMA DURING THE WEEK OF JULY 8, 1984,

That the Association does hereby request and recommend to the United States Congress that it adopt the Amendment, set out below, to the Employee Retirement Income Security Act:

"An Act to amend and clarify ERISA by adding a second and thrid sentence to section 514(a), 29 U.S.C. §1144(a):

State laws prohibiting employers from discriminating in the provision of employee benefits, obligating employers to pay promised employee welfare benefits to its employees and providing for the enforcement of such obligations shall not be considered laws relating to an employee benefit plan. The foregoing sentence shall not apply to employee pension benefit plans."

Be it further resolved that a copy of this amendment be sent to the President, the Secretary of Labor, and to all members of Congress at their convening in 1985.

STATEMENT OF INTEREST OF AMICUS CURIAE

This memorandum of law is submitted on behalf of amicus curiae State of New York pursuant to Rule 29 of the Federal Rules of Appellate Procedure in support of the appeal by Intervenor-Plaintiff-Appellant John C. Brooks, Commissioner of Labor of the State of North Carolina, from the decision of the United States District Court for the Middle District of North Carolina. Joining in this brief as amici urging reversal of the district court's decision are the District of Columbia and the States of Alaska, Connecticut, Hawaii, Illinois, Maryland, Montana, Oklahoma, Vermont and Wisconsin.

The district court held that North Carolina's application of its Wage and Hour Act (N.C. Gen. Stat., Ch. 95, Art. 2A) ("Act") to Defendant-Appellee Burlington Industries, Inc.'s severance pay policy is preempted by the Employee Retirement Income Security Act of 1974, as amended ("ERISA"), 29 U.S.C. § 1001 et seq., because Burlington's policy constitutes an "employee benefit plan" covered by ERISA and the Act "relate[s] to" the policy within the meaning of ERISA's preemption provision, § 514, 29 U.S.C. § 1144.

The issues raised by this appeal are of critical importance to the State of New York and the ten other amici, all of which have wage and benefit enforcement legislation

Exhibit B

similar to that which the district court in North Carolina invalidated as pre-empted.* The statute invalidated by the district court, N.C. Gen. Stat. § 95-25.7, provides that employers who have contractually agreed to pay certain wages to their employees must pay those wages promptly after termination of the employment relationship. North Carolina's Wage and Hour Act establishes an administrative process that begins with the filing of a complaint and an administrative investigation by the State Department of Labor. If the investigator concludes that the complaint is meritorious, then conciliation efforts are initiated. If conciliation is unsuccessful, then a hearing is held, followed by a determination by the State Department of Labor as to the merits of the wage claim. If an employer refuses to pay a claim which the agency has upheld, the employee(s) or the State Commissioner of Labor may bring a civil action to recover the unpaid wages. "Wages" are defined to include, inter alia, severance pay. See N.C. Gen. Stat. § 95-25.2(16).

* One provision of New York's wage enforcement legislation, N.Y. Labor Law § 198-c, is being challenged by Burlington in related litigation in New York. See Gilbert v. Burlington Industries, Inc., No. 83-6954 (S.D.N.Y. Sept. 17, 1984), appeal docketed, Nos. 84-7824, 84-7908 (2d Cir.).

The wage and benefit enforcement laws of the amici are described in a summary which is annexed to this brief as an appendix.

North Carolina's Wage and Hour Act is not unique. Forty-seven other states have similar statutes enforcing employers' wage and benefit payment obligations.* Most of these statutes, like North Carolina's, require employer compliance with severance pay agreements and create state administrative mechanisms to enforce them. The continued viability of these state wage and benefit enforcement schemes is jeopardized by the district court's determination, since, if it is upheld, the states will be precluded from carrying out their traditional and routine wage and hour enforcement responsibilities whenever employers fail to keep their promises to employees to pay severance benefits.

In addition, the district court's expansive reading of ERISA's preemption provision and definition of an "employee benefit plan" threatens many other state statutes which in some way involve or touch upon employee benefits. By reading ERISA's definition of benefit plan out of the context of ERISA's entire legislative framework and history, the district court interpreted that section to include mere promises, consisting of no more than written statements of policy that have no identity apart from the employer itself. The court's holding equally could be applied to promises to provide periodic or occasional training, or even child care, since ERISA's definition of a benefit plan expressly encompasses plans

* The only states lacking such legislation are Florida and Mississippi. See State Labor Laws, BNA Labor Relations Reporter (1984).

that provide such benefits. More important, under the court's view of ERISA's preemption provision, numerous state statutes which, for example, establish training standards or require minimum skills in order to be licensed to work in certain trades might be preempted whenever they remotely "relate to" an employment apprenticeship program.

Today, an employee's compensation consists of much more than regular wages or salary. Thus, a finding of preemption in this case would result in subjecting most aspects of employee compensation, excluding only the simple payment of an employee's regular wages or salary, to federal regulation and supervision. Every employer payroll policy providing paid time-off, such as vacation, holiday, sick or maternity leave, could as a consequence be subject to ERISA's massive regulatory framework and every employer, large and small, could be brought into federal court to justify a simple personnel decision.

Congress never intended such a radical intrusion into an area historically reserved for local control. Nor would the purpose of ERISA, to protect employees' rights to benefits and to encourage the growth of multistate plans by preempting conflicting state regulation, be served by completely barring state enforcement of employer promises to pay wages and benefits. The State of New York and the amici joining in this brief urge this Court to reverse the district court's decision.

ARGUMENT

I. ERISA DOES NOT PREEMPT THE STATES' AUTHORITY TO EXERCISE THEIR TRADITIONAL POLICE POWERS TO ENFORCE EMPLOYER PROMISES TO PAY EMPLOYEE WAGES AND BENEFITS

A. State Wage And Benefit Enforcement Legislation, Such As N.C. Gen. Stat. § 95-25.7, Is An Exercise Of The State's Police Power Which May Not Be Preempted Unless Congress Clearly Expresses Such An Intent

One of the powers reserved to the states under the Tenth Amendment to the Constitution is the state's "police power". Keller v. U.S., 213 U.S. 136 (1909); License Cases, 5 How. 504, 576-77, 12 L.Ed. 256, 289 (1847); Gibbons v. Ogden, 9 Wheat. 1, 206, 6 L.Ed. 23, 72 (1824). A state's exercise of its traditional police powers in an area of local concern may not be preempted by federal law in the absence of a clearly expressed congressional intent to do so. As the United States Supreme Court stated: "when a State's exercise of its police power is challenged under the Supremacy Clause, 'we start with the assumption that the historic police powers of the States were not to be superseded by the Federal Act unless that was the clear and manifest purpose of Congress.'" Ray v. Atlantic Richfield Co., 435 U.S. 151, 157 (1978), quoting Rice v. Santa Fe Elevator Corp., 331 U.S. 218, 230 (1947). Accord Alessi v. Raybestos-Manhattan, Inc., 451 U.S. 504, 522 (1981); Reid v. Colorado, 187 U.S. 137, 146 (1902); Rebaldo v. Cuomo, No. 84-7386, slip op. at 6944 (2d Cir. Nov. 26, 1984); Stone v.

Exhibit C

Stone, 450 F. Supp. 919, 932-33 (N.D.Cal. 1978), aff'd, 632 F.2d 740 (9th Cir. 1980), cert. denied, 453 U.S. 922 (1981).*

The judicial concern for accommodating state authority in areas of local responsibility is so strong that even in fields totally occupied by federal regulation state action may be upheld if the subject of state action "is of only peripheral concern to the federal law or touches interests deeply rooted in local feeling and responsibility." Belknap, Inc. v. Hale, ____ U.S. ____, ____, 103 S.Ct. 3172, 3177 (1983) (National Labor Relations Act does not preempt common law causes of action for misrepresentation and breach of contract). In such cases, the state's interest in the subject matter prevails if it is weightier than the potential interference with the federal regulatory scheme and the risk that the state will sanction conduct that the federal legislation protects. Id. See also Farmer v. United Brotherhood of Carpenters, 430 U.S. 290, 302 (1977) ("inflexible application of the [preemption] doctrine is to be avoided, especially where the State has a substantial interest in regulation of the conduct at issue and the state's interest is one that does not threaten undue interference with the

* The purpose of this rule is to ensure "that 'the federal-state balance' ... will not be disturbed unintentionally by Congress or unnecessarily by the courts." Jones v. Rath Packing Co., 430 U.S. 519, 525 (1977) (citation omitted).

federal regulatory scheme").*

Adherence to these principles is critical, since they establish the framework for construing ERISA's apparently broad preemption provision. The district court's failure to give due respect to them in this case resulted in a decision that not only is incorrect, but, if affirmed, could have disastrous consequences for states' ability to legislate in a host of health and safety areas as to which Congress plainly did not intend preemption.**

* This rule has been applied in several ERISA preemption cases. See, e.g., Providence v. Valley Clerks Trust Fund, 509 F. Supp. 388, 391 (E.D.Cal. 1981) ("where the state law has only an indirect effect on [an employee benefit] plan and where it is one of general application which pertains to an area of important state concern, the court should find there has been no preemption") (emphasis in original); Deiches v. Carpenters' Health and Welfare Fund, 572 F. Supp. 766, 771 (D.N.J. 1983).

** For example, ERISA's definition of "employee benefit plan" in § 3(1) and (3), 29 U.S.C. § 1002(1) and (3), specifically refers to plans providing apprenticeship and training programs. Yet many states, pursuant to their police power, require participation in apprenticeship or training programs as a pre-condition for obtaining a license to work in a wide variety of jobs and trades, ranging from motion picture operators to plumbers, electricians and nurses. See, e.g., N.Y. Gen. City Law §§ 18 and 20(27). Many such laws demand that certain subjects be taught in these programs. Similarly, New York, like some other states, requires employers to train their employees in the handling of toxic substance. See N.Y. Labor Law §§ 875-878. The logic of the district court's decision could be read to invalidate all such health and safety legislation to the extent that the training is provided as an employee benefit.

ERISA's definition of "employee benefit plan" also includes plans providing day care services for employees' children. Many states regulate day care centers. See, e.g., N.Y. Soc. Serv. Law § 390. Again, under the district court's view of ERISA's preemption provision, the states would be precluded from regulating such services to the extent that they are provided as an "employee benefit plan."

Unquestionably, § 95-25.7 of North Carolina's Wage and Hour Act, like similar legislation in almost every other state, constitutes an exercise of the State's police power in a field historically reserved for local control. The goal of such legislation is clear: to promote the health, safety and welfare of the State's citizens by protecting them from unscrupulous employer practices.* As the New York Court of Appeals stated with respect to New York's wage and benefit enforcement legislation: "[t]he purpose of the law was to assure prompt payment of daily wages to those employed in a subordinate capacity and who depended upon their earnings for support... ." People v. Vetri, 309 N.Y. at 405, 131 N.E.2d at 570. See also People v. Grass, 257 A.D. 1, 3, 11 N.Y.S.2d 803, 805 (1st Dep't 1939); 1912, Op. N.Y.S. Att'y Gen. 538, 539.**

Such legislation falls squarely within the traditional police powers of the State. As the Supreme Court recently reaffirmed: "[s]tates possess broad authority under their police powers to regulate the employment relationship to

* Such legislation has existed and been enforced for many decades. For example, New York Labor Law § 191, the State of New York's wage enforcement statute comparable to N.C. Gen. Stat. § 95-25.7, derives from legislation (former §§ 196 and 196-c of the Labor Law) which has its origin in statutes first adopted in 1890. See People v. Vetri, 309 N.Y. 401, 405, 131 N.E.2d 568, 570 (1955); 1906, Op. N.Y.S. Att'y Gen. 448.

** Employee compensation usually consists of much more than simple wages or salary, and most states so recognize by including benefits such as severance pay within their statutory definition of wages.

protect workers within the State." De Canas v. Pica, 424 U.S. 351, 356 (1976); see also West Coast Hotel Co. v. Parrish, 300 U.S. 379 392-94 (1937).^{*} The subject is so deeply rooted in local responsibility that the United States Court of Appeals for the Second Circuit recently characterized New York State's interest in regulating employer-employee relations as "compelling" and "essential to the preservation of industrial peace and a sound economic order". Catholic High School Ass'n v. Culvert, No. 83-9013, slip op. at 7149-50 (2d Cir. Jan. 10, 1985).

Accordingly, ERISA does not preempt legislation such as N.C. Gen. Stat. § 95-25.7 unless its language or legislative history reveals a clear and manifest congressional intent to do so.

^{*} Indeed, the Supreme Court has upheld, against constitutional challenge, New York's earliest wage enforcement legislation in part on the ground that it was a valid exercise of the State's police power. Erie Railroad Co. v. Williams, 233 U.S. 685, 702-704 (1914). See also New York Central & Hudson River R.R. v. Williams, 64 Misc. 15, 27-28 (Sup.Ct., Albany Co.), aff'd, 136 A.D. 904, (3d Dep't 1909), aff'd, 199 N.Y. 108 (1910); People v. Vetri, 309 N.Y. at 405, 131 N.E.2d at 570 ("Section 196 of the Labor Law is a police power regulation intended for the protection of those who are dependent upon their wages for sustenance").

B. Congress Did Not Intend To Preclude The States From Exercising Their Police Power To Enforce Employer Promises To Pay Wages And Benefits To Their Employees

Nothing in the language of ERISA's preemption provision or legislative history offers even a hint, let alone a clear expression, of a congressional intent to nullify the wage and benefit enforcement legislation of forty-eight states. In fact, the legislative history of ERISA demonstrates that Congress considered that such legislation involved completely different problems and remedies than those with which Congress was concerned in enacting ERISA. Congress only sought to preclude states from regulating the terms and conditions of employee benefit plans (*i.e.*, the types of benefits provided or the structure, administration or internal rules and regulations of such plans), since such regulations could create conflicting mandates inhibiting or interfering with the establishment of interstate benefit plans.

1. Congress Did not Consider State Wage And Benefit Enforcement Legislation As Relevant To ERISA Plans, And Therefore Congress Had No Intent To Invalidate Such Legislation

In enacting ERISA, Congress' concern was not with the enforcement of employers' wage and benefit promises, which had been effectively policed for many years -- in some instances for over three-quarters of a century -- by nearly every state in the country. Instead, the focus of Congress' attention was "a relatively modern economic institution" which had

experienced "phenomenal expansion" in the years following World War Two. H.R. Rep. No. 93-533, 93rd Cong., 2d Sess. ("House Rep.") at _____, reprinted in 1974 U.S. Code Cong. & Admin. News 4639 ("Legis. Hist."), at 4640-41. Accord S. Rep. No. 93-127, 93rd Cong., 2d Sess. ("Senate Rep.") at _____, reprinted in Legis. Hist. at 4839-40.

The recent and burgeoning economic development with which Congress was concerned obviously was not simple employer promises to pay wages and benefits such as severance pay. Congress was concerned with the complex arrangements being established by employers, unions, and both jointly, to provide for the payment of pensions, annuities, medical and other benefits through "plans" and funds which enjoyed a status separate and distinct from either the employers or the unions.

Far from being the historic subject of state regulation, these "plans" were hardly regulated at all, as Congress knew. The House Report states: "[t]he growth and development of the private pension system in the past two decades has been substantial. Yet, regulation of the private system's scope and operation has been minimal and its effectiveness a matter of debate." Legis. Hist. at 4641 (emphasis added); accord Senate Rep. at _____, Legis. Hist. at 4840. Moreover, the House and Senate Reports make clear that

Congress viewed the existing "minimal" regulation as consisting almost exclusively of federal regulation. Both the House and the Senate Reports describe at length the regulatory effects on welfare and pension plans of the National Labor Relations Act of 1935, the Labor Management Relations Act of 1947, the Welfare and Pension Plans Disclosure Act of 1958, the Labor Management Reporting and Disclosure Act of 1959, and the Internal Revenue Code of 1954. See Legis. Hist. at 4641-42 and 4840-41.

Indeed, one of the principal problems that Congress sought to rectify was the inadequacy of this patchwork of federal statutes to curb the abusive practices that had plagued complex benefit plan arrangements. As the House Report states: "[i]n the absence of adequate federal standards, the participant is left to rely on the traditional equitable remedies of the common law of trusts", which were ill-suited and ineffective in dealing with these "modern economic institutions" established to provide employee benefits. Legis. Hist. at 4643. Employees could not rely on common law principles of contract, since the employees' only contractual relationship was with their employers -- not with the separate and distinct entities which their employers had established to provide benefits.

ERISA's legislative history contains virtually no discussion of existing state legislation, because few state statutes governed the area of congressional concern. The only reference to applicable state legislation consists of the observation that only "[a] few states...have codified existing trust principles and enacted legislation" to address the unique problems of these benefit plan arrangements. House Rep. at ____; Legis. Hist. at 4643. These state laws, the House Report notes, were limited to simple disclosure requirements, similar to those already required by federal law. Id.

Congress thus did not consider that the numerous and long-standing statutes exercising the states' police power to enforce employer promises to pay wages and benefits had any bearing whatsoever on the plan arrangements to be covered by ERISA. Congress plainly viewed the subjects of ERISA regulation as a recent development which, due to its novelty, lacked any state supervision and was subject only to inadequate federal legislation and common law trust principles.*

* That Congress did not believe that existing state wage and benefit legislation had any relevance to ERISA plans is further demonstrated both by the complete absence of any legislative debate over the effect of ERISA preemption on any of the various police power statutes, and by the substance of the few comments on preemption that can be found in the legislative history. Those comments indicate that Congress was primarily concerned with future attempts by the states to regulate benefit plan arrangements, since few state statutes were then in existence. For example, Senator Javits explained that the preemption clause served to avoid "opening the door to multiple and potentially conflicting State laws hastily contrived to deal with some particular aspect of private welfare or pension benefit plans..." 120 Cong. Rec. 29942 (1974).

Since Congress did not consider the extensive network of state legislation enforcing employer wage and benefit promises to have any relevance to the problems addressed by ERISA, Congress could not have intended ERISA to obliterate long-standing state authority to police such promises. Therefore, not only is Congress' intent to preempt such laws not "clear and manifest", it is simply non-existent.

2. ERISA's Preemption Provision Invalidates Only Those State Laws Which "Regulate" The "Terms And Conditions" Of Benefit Plans

ERISA's preemption provision, § 514(a), states that ERISA "shall supersede any and all State laws insofar as they may now or hereafter relate to any employee benefit plan." See 29 U.S.C. § 1144(a). Significantly, the term "State" is defined in § 514(c)(2) so as to narrow the apparently sweeping scope of the provision:

The term "State" includes a State, any political subdivisions thereof, or any agency or instrumentality of either, which purports to regulate, directly or indirectly, the terms and conditions of employee benefit plans covered by this Title.

See 29 U.S.C. § 1144(c)(2) (emphasis added).

Thus "a state law must 'purport[] to regulate,... the terms and conditions of employee benefit plans' to fall within the preemption provision." Rebaldo v. Cuomo, slip op. at 6943. See also Stone & Webster Engineering Corp. v. Ilesley,

690 F.2d 323, 329 (2d Cir. 1982), aff'd sub nom. Arcudi v. Stone & Webster Engineering Corp., ____ U.S. ____, 103 S.Ct. 3564 (1983). The meaning of this restrictive language is made clear by ERISA's legislative history and by judicial decisions applying the preemption provision. Both demonstrate that Congress' purpose was to supersede only those state laws which attempt to regulate the internal rules and regulations or administration of a plan (e.g., reporting, disclosure, fiduciary responsibilities), a task which ERISA reserves to itself, or those state laws which seek to define, prescribe or prohibit the types of benefits offered by the plan, a task which ERISA leaves to the discretion of the plan designers and administrators.

Federal preemption was based upon Congress' principal concern that state attempts to regulate benefit plans might impede the growth of multi-state plans by imposing conflicting requirements for the plans' structure, administration or provision of benefits. As then Secretary of Labor Shultz stated with respect to benefit plan legislation being considered by the House in 1970, exclusive regulation by the federal government would ensure that "[a]dministrators of plans covering employees in several or more states will not have the burden of complying with several sets of state laws, rules and regulations. They will be able to formulate procedures and conduct themselves with reference to one uniform law." See

SELECTED PROVISIONS OF ARTICLE 2A
OF CHAPTER 95,
NORTH CAROLINA GENERAL STATUTES

§ 95-25.2. Definitions.

In this Article, unless the context otherwise requires:

- (16) "Wage" paid to an employee means compensation for labor or services rendered by an employee whether determined on a time, task, piece, job, day, commission, or other basis of calculation, and the reasonable cost as determined by the Commissioner of furnishing employees with board, lodging, or other facilities. For the purposes of G.S. 95-25.6 through G.S. 95-25.12, "wage" includes sick pay, vacation pay, severance pay, commissions, bonuses, and other amounts promised when the employer has a policy or a practice of making such payments.

§ 95-25.6. Wage payment.

Every employer shall pay every employee all wages and tips accruing to the employee on the regular payday. Pay periods may be daily, weekly, bi-weekly, semi-monthly, or monthly. Wages based upon bonuses, commissions, or other forms of calculation may be paid as infrequently as annually if prescribed in advance. (1975, c. 413, s. 3; 1977, c. 826, s. 3; 1979, c. 839, s. 1.)

§ 95-25.7. Payment to separated employees.

Employees whose employment is discontinued for any reason shall be paid all wages due on or before the next regular payday. Wages based on bonuses, commissions or other forms of calculation shall be paid on the first regular payday after the amount becomes calculable when a separation occurs. Such wages may not be forfeited unless the employee has been notified in accordance with G.S. 95-25.13 of the employer's policy or practice which results in forfeiture. Employees not so notified are not subject to such loss or forfeiture. (1975, c. 413, s. 4; 1979, c. 839, s. 1; 1981, c. 663, s. 1.)

§ 95-25.12. Vacation pay.

No employer is required to provide vacation for employees. However, if an employer provides vacation for employees, the employer shall give all vacation time off or payment in lieu of time off in accordance with the company policy or practice. Employees shall be notified in accordance with G.S. 95-25.13 of any policy or practice which requires or results in loss or forfeiture of vacation time or pay. Employees not so notified are not subject to such loss or forfeiture. (1979, c. 839, s. 1; 1981, c. 663, s. 6.)

§ 95-25.15. Investigations and inspection of records; notice of law.

(a) The Commissioner or his designated representative shall have the power and authority to enter any place of employment and gather such facts as are essential to determine whether or not the employer is covered by any provision of this Article.

With respect to any provision of this Article under which the employer is covered, the Commissioner or his designated representative may inspect such places and such records, make transcriptions of any and all such records, question employees and investigate such facts, conditions, practices, or matters as are necessary to determine whether the employer has violated said provision of this Article.

With respect to the provisions of G.S. 95-25.6 through 95-25.12 (Wage Payment) as those provisions apply to persons covered by the Fair Labor Standards Act, the Commissioner or his designated representative shall have no authority under this subsection unless the Commissioner or his designated representative has received a complaint from an employee of the covered establishment, and then shall investigate that specific complaint only.

(b) Except as otherwise provided in this Article, every employer subject to any provision of this Article shall make, keep, and preserve such records of the persons employed by the employer and of the wages, hours, and other conditions and practices of employment which are essential to the enforcement of this Article and are prescribed by regulation of the Commissioner, except that the Commissioner shall have no authority to prescribe records for the State of North Carolina, a city, town, county or other municipality or agency or instrumentality of government.

(c) A poster summarizing the major provisions of this Article shall be displayed in every establishment subject to this Article. (1937, c. 317, ss. 5, 19; 1959, c. 475; 1971, c. 1231, s. 2; 1973, c. 649, s. 4; 1975, c. 413, ss. 7, 9; 1979, c. 839, s. 1.)

§ 95-25.16. Enforcement.

(a) The Commissioner shall enforce and administer the provisions of this Article, and the Commissioner or his authorized representative is empowered to hold hearings and to institute criminal and civil proceedings hereunder.

(b) The Commissioner or his authorized representative shall have power to administer oaths and examine witnesses, issue subpoenas, compel the attendance of witnesses and the production of papers, books, accounts, records, payrolls, documents, and take depositions and affidavits in any proceeding hereunder. (1937, c. 317, s. 19, c. 409, s. 7; 1971, c. 1231, s. 2; 1973, c. 649, s. 4; 1975, c. 473, s. 9, c. 475; 1979, c. 839, s. 1.)

§ 95-25.22. Recovery of unpaid wages.

(a) Any employer who violates the provisions of G.S. 95-25.3 (Minimum Wage), G.S. 95-25.4 (Overtime), or G.S. 95-25.6 through 95-25.12 (Wage Payment), shall be liable to the employee or employees affected in the amount of their unpaid minimum wages, their unpaid overtime compensation, or their unpaid amounts due under G.S. 95-25.6 through 95-25.12, as the case may be.

In its discretion, the court may award exemplary damages in an amount not in excess of the amount found to be due as provided above.

(b) Action to recover such liability may be maintained in the General Court of Justice by any one or more employees.

(c) Action to recover such liability may also be maintained in the General Court of Justice by the Commissioner at the request of the employees affected. Any sums thus recovered by the Commissioner on behalf of an employee shall be held in a special deposit account and shall be paid directly to the employee or employees affected.

(d) The court, in any action brought under this section may, in addition to any judgment awarded plaintiff, order costs and fees of the action and reasonable attorneys' fees to be paid by the defendant.

The court may order costs and fees of the action and reasonable attorneys' fees to be paid by the plaintiff if the court determines that the action was frivolous.

(e) The Commissioner is authorized to determine and supervise the payment of the amounts due under this section, and the agreement to accept such amounts by the employee shall constitute a waiver of the employee's right to bring an action under subsection (b) of this section.

(f) Actions under this section must be brought within two years pursuant to G.S. 1-53.

(g) Prior to initiating any action under this section, the Commissioner shall exhaust all administrative remedies, including giving the employer the opportunity to be heard on the matters at issue and giving the employer notice of the pending action. (1959, c. 475; 1975, c. 413, s. 11; 1979, c. 839, s. 1.)

Exhibit E

NORTH CAROLINA

Employees thus have an access to remedies, including recovery of unpaid wages, which simply would not exist if ERISA applied to general practices and preempted the state laws. The situation of wage earners in North Carolina exemplifies this fact.³ It is a good thing that state laws to pay an employee all vacation wages due the employee has two avenues available to him. He can file suit on his own in state court under the North Carolina Wage and Hour Act, or he can file a complaint with the Wage and Hour Division of the North Carolina Department of Labor. If he chooses the latter, the employee draws on the resources of an administrative agency with eighteen compliance officers stationed throughout the state whose primary function is to investigate and conciliate wage payment complaints. Should an employer refuse to pay a claim substantiated by a compliance officer, an administrative process commences which includes an opportunity for a hearing and a final agency determination. If the final decision upholds the claim and the employer still refuses to pay, the employee may request the Department of Labor to file a lawsuit on his behalf to recover the unpaid wages and exemplary damages. The North Carolina Wage and Hour Division investigated over 2,000 such complaints a year and answers the questions of many other potential defendants and employers before a problem develops.

Exhibit F

NEW YORK

The New York Wage and Benefit Payment Statute is similar but not identical to North Carolina's. It provides several avenues for an employee to recover unpaid wages and benefits and a range of remedies, thereby insuring to the greatest extent possible that employees receive their wages and benefits. Article 6 of the New York Labor Law, which governs the obligation of employers to pay wages and benefits, does not require an employer to pay any particular wages or benefits, but only to pay those it has agreed to pay by policy or practice. An employee who is not paid the agreed upon wages or benefits may in New York, as in North Carolina, either file a claim for the monies owed with the New York State Department of Labor or institute a civil action in State court to recover the monies.

The administrative processing of an employee's claim is expeditious and fairly routine; in New York State there are presently about 75 investigators who investigate wage and benefit claims in addition to other labor law violations. If the investigation establishes a violation, a compliance conference is scheduled where both the employer and the employee may appear. If no informal resolution is reached, the Commissioner of Labor issues an Order to Comply for the amount found to be due the employee. Under New York law the Order to Comply must include interest of not less than 6%, and may include a civil penalty in the amount of 25% of the total amount due. An Order to Comply

can be filed with the courts. If a claim is not enforced without further proceedings, it is fatal, either the commissioner or an employee has commenced a claim with respect to benefit claim in court. If the claim is enforced, the court will award costs and the court must award attorney's fees. In the event the court finds that the failure to pay wages or benefits is willful, it may award trebled damages. See, generally, Art. 6, New York Labor Law.

New York law also makes it a misdemeanor to fail to pay wages and benefits and imposes criminal liability on any individual officers, agents, or shareholders of any employer who knowingly permit a corporation to violate the law. Any of the remedies provided for under New York Labor Law may be enforced simultaneously. The New York State Department of Labor investigates about 3,400 wage and benefits claims per year involving 2,000 employers. See, §198-c, New York Labor Law.

Exhibit G

SUMMARY DESCRIPTION OF WAGE PAYMENT LAWS OF ALASKA,
CONNECTICUT, DISTRICT OF COLUMBIA, HAWAII, ILLINOIS, MARYLAND,
MONTANA AND OKLAHOMA, VERMONT AND WISCONSIN

ALASKA

Alaska has two wage collection statutes. One provides specifically for actions arising from violations of the minimum wage and/or overtime laws. This statute is commonly referred to as the "Alaska Wage and Hour Act," and closely parallels the FLSA, 1933, as amended. See AS 23.10.030--.150.

The second statute relates to wage claims, in general. See AS 23.05.140--.260. This statute is very similar to the North Carolina and New York statutes in its content and administration. Claims accepted under this statute involve the contractual aspect of employment which deal with fringe benefits, primarily vacation or severance pay. An Alaska wage earner may choose a civil remedy either through the resources of the department or on his own under a workman's independent right of action. The second remedy is exclusively used where the wages or benefits in question exceed the department's statutory minimum, exclusive of penalties, of \$3000. The department has the authority to use internal administrative adjudication processes to resolve complaints. These processes, however, are not obligatory and we may move a claim directly into the courts for a final solution.

The courts are generally reserved for serious disputes or for employers subject to recidivism. Most claims are handled quickly using one or more informal conferences involving an investigator, the claimant, and the employer or employer representative.

SUMMARY DESCRIPTION OF WAGE PAYMENT LAWS OF ALASKA,
CONNECTICUT, DISTRICT OF COLUMBIA, HAWAII, ILLINOIS, MARYLAND,
MONTANA AND OKLAHOMA, VERMONT AND WISCONSIN

ALASKA

Alaska has two wage collection statutes. One provides specifically for actions arising from violations of the minimum wage and/or overtime laws. This statute is commonly referred to as the "Alaska Wage and Hour Act," and closely parallels the FLSA, 1938, as amended. See AS 23.10.050--.150.

The second statute relates to wage claims, in general. See S 23.05.140--.260. This statute is very similar to the North Carolina and New York statutes in its content and administration. Claims accepted under this statute involve the contractual aspect of employment which deal with fringe benefits, primarily vacation or severance pay. An Alaska wage earner may choose a civil remedy either through the resources of the department or on his own under a workman's independent right of action. The second remedy is exclusively used where the wages or benefits in question exceed the department's statutory minimum, exclusive of penalties, of \$5000. The department has the authority to use internal administrative adjudication processes to resolve complaints. These processes, however, are not obligatory and we may move a claim directly into the courts for a final solution.

The courts are generally reserved for serious disputes or for employers subject to recidivism. Most claims are handled quickly using one or more informal conferences involving an investigator, the claimant, and the employer or employer representative,

frequently an attorney. The more formal hearing process is reserved for fact finding to clarify complicated questions of law, or to determine if criminal as well as civil sanctions are in order.

In Alaska there are currently 12 investigators and 4 technicians who investigate claims for wages and benefits or enforce other labor laws. The department investigates and resolves 1600 claims per year with the average resolution time, outside of court, being 5 months. It may take from 7 months to 2 years to litigate a claim depending on the amount of the claim and legal complexities which dictate whether the matter will be heard at the district or superior court level. About 10 percent of our cases require formal litigation for resolution. The department's resources are without charge to the claimant while legal fees in the private sector begin at about \$85 per hour.

CONNECTICUT

The Connecticut Commissioner of Labor, through the Department of Labor, Division of Regulation of Wage, oversees enforcement of Connecticut's wage payment laws, sections 31-71a through 31-71i, 31-72 and 31-76k, Connecticut General Statutes. Specifically, §31-76k requires an employer to pay terminated employees all accrued fringe benefits where the employer has a policy or is party to a collective bargaining agreement providing for payment of such benefits upon termination. The fringe benefits covered by section 31-76k include vacations,

holidays, sick days and severance pay. When the Department of Labor receives a complaint from a terminated employee that promised fringe benefits have not been paid, it engages in an administrative investigation through the mails or in person using one of its six Wage Employment Agents. An administrative hearing may be held if necessary to determine disputed issues. When it determines that an employer has unlawfully failed to pay fringe benefits, the Department of Labor can initiate either a criminal action §31-71g or a civil action under §31-72 to collect double damages.

DISTRICT OF COLUMBIA

The District of Columbia Wage Payment and Wage Collection Law, 36 D.C. Code §§101-110 (1981 ed.) enacted by Congress in 1956, (70 stat. 976) requires employers to make timely payment of wages to employees employed in the District of Columbia.

When an employer fails to pay wages (including vacation pay and severance pay) as required, an aggrieved employee has two recourses: he or she may file an action in court to recover the unpaid wages and liquidated damages, or file a complaint with the Office of Wage-Hour, D.C. Department of Employment Services. If the employee chooses the latter course, the employer is notified by letter of the filing of the complaint and the date and time of an administrative hearing. If a determination is made that the employer is in violation of the law, and refuses to pay the wages

found due, the case is transferred to the Corporation Counsel of the District of Columbia for filing of criminal charges or a civil action.

With a staff of 4 wage-hour compliance specialists assigned to investigate complaints and conducting administrative hearings, the staff during the past 5-years (1980-84) has processed 4,564 complaints from employees alleging violation of the Wage Payment and Wage Collection Law. Slightly more than 1 million dollars has been recovered in unpaid wages and damages for employees.

HAWAII

In Hawaii, an employee who is not paid all wages due may either file a claim with the State of Hawaii's Department of Labor and Industrial Relations or bring a civil action in a state court to recover any monies owed.

The Department of Labor and Industrial Relations, under the statutes and administrative rules and regulations relating to the Payment of Wages and Other Compensation Law, Chapter 388, Hawaii Revised Statutes, investigates and conciliates unpaid wage claims including vacation, sick, and severance pay. The law does not require the employer to pay any set amount as pay and benefits but only to pay what the employer has promised to pay to the employee. If, after an investigation substantiating a claim for unpaid wages or other compensation is completed and the employer fails or refuses to pay the employee, the Department of Labor and

Industrial Relations may file a lawsuit on the employee's behalf to collect the amounts owed. If the Department prevails in the lawsuit, the Department may recover, in addition to the unpaid wages, a penalty in an amount up to the amount of the wages due. The court must also order the employer to pay the costs of bringing the action and reasonable attorney's fees.

When the employee brings a civil suit, the employee, too, may recover the civil penalties as well as the costs and reasonable attorney's fees.

The statute also provides for criminal penalties. It is a misdemeanor for any employer to fail to pay wages under the Payment of Wages and Other Compensation Law or for any officer of a corporation to knowingly permit the corporation to fail to pay wages. The employer or officer is subject to a fine of not less than \$100 or more than \$10,000.

Seven investigators investigate and conciliate the approximately 1,200 claims which are filed each year with the Department. Approximately 90 cases were referred to the Attorney General for legal action during the last completed fiscal year.

Any complaint filed under ERISA is not accepted here in Hawaii but must be filed in Washington, D.C. with the Division of Inquiries and Technical Assistance. Whether or not prompt action is taken on these complaints is not known. Therefore, it is very important to the people of Hawaii that the Payment of Wages and Other Compensation Law continue to be applicable in the area of wages and benefits.

ILLINOIS

The Wage Claim Division of the Illinois Department of Labor is responsible for enforcing the Wage Payment and Collection Act, Ill. Rev. Stat., Ch. 48, pars. 39m-1 to 39m-16 (1983).

Section 2 of the Act includes in its definitions of "wages" and "final compensation" "any compensation owed an employee by an employer pursuant to an employment contract or agreement between the 2 parties." Even before this language was added to the statute, an Illinois appellate court construed the Act as covering severance pay claims. See, Metropolitan Distributors, Inc. v. Illinois Department of Labor, 449 N.E. 2d 1000 (Ill. App. 1983) (copy enclosed).

Section 11 of the Act outlines the duties and powers of the Department, which include the authority to take assignments of wage claims and proceed civilly and to cause criminal complaints to be prosecuted. The statute also preserves a private right of action.

Workers who want to file a claim for wages or final compensation fill out a short application form. If the division has jurisdiction, it writes to the worker's employer and asks for payment or a written response to the claim.

If the employer fails to respond, or if the worker disputes the response, the Wage Claim Division schedules a hearing in one of nine cities: Chicago, Springfield, Rockford, Peoria, Champaign, Marion, Collinsville, Rock Island or Effingham.

At the hearing, a labor conciliator listens to both sides and examines any witnesses or written evidence. If the worker and employer do not reach a voluntary settlement, the conciliator either dismisses the claim or issues a demand for payment.

If the employer fails to comply with this demand, the division institutes prosecution. An employer convicted of violating the Wage Payment and Collection Act can be sentenced to 30 days in jail or fined \$500.00 for each day on which a violation occurs.

During the fiscal year ending June 30, 1984, the Illinois Department of Labor received 10,528 wage complaints claiming \$15,498,980 due. Of this amount \$3,786,232 involved vacation pay, severance pay or other fringe benefits. The Department held 8,827 hearings on wage claims during that year and resolved complaints involving \$13,977,315. All of this was accomplished with a staff of fourteen.

MARYLAND

The intent of the Maryland Wage Payment and Collection Law was to provide a quick, simple method for employees to collect monies which were due them for services performed without cost to the employee. There are, of course, other remedies available to employees. These remedies are, in most instances, time-consuming and involve either considerable cost to the employee or require certain knowledge which the employee does not have. A court date for a civil suit in the lowest state court is usually two to three

months in the future. A fee of \$250.00 is the minimum charged by an attorney to prepare and litigate even the simplest civil suit. Even with the ~~loose~~ and informal procedures in the "small claims court", the employee generally does not have the knowledge to pursue his claim.

The vast majority of claims are for relatively small amounts, usually two weeks pay or less. The claimants are generally in the lowest paid jobs, many working at minimum wage. In 1983, the average amount collected per valid claim was \$297.18.

The nature of these claims mandates that they be resolved as quickly as possible. The vast majority of cases are resolved within 30 days. An administrative assistant and two clerical employees conduct the office functions, office and field functions are supervised by a Wage and Hour Investigator Supervisor. Approximately 40 percent of all claims are investigated by three specialists; the remainder are assigned to 16 other investigators in their areas of residence. Generally, the issues involved are emotional, requiring the investigator to exercise extreme tact and diplomacy to resolve the claim quickly and to the reasonable satisfaction of both parties. Because of the variety of employers involved, each investigator must have a broad business background.

The Wage Payment and Collection Law is codified as Article 100, Section 94, Annotated Code of Maryland. Subsection 94(a)(3) defines wages as "any remuneration, compensation, bonus, commission, and/or fringe benefit promised in return for services by an employee". By administrative decision, vacation pay,

holiday pay, severance pay, pension payments, insurance payments and any and all fringe benefits are included in the definition of wages. Simply stated, the employee must get what he was promised and this agency stands available to investigate all claims of non payment of promised monies.

A Wage Payment and Collection claim usually is initiated by a telephone call from an employee: "My boss won't pay me what he owes me". Two claims forms, one a condensed version of the other, are mailed to the employee. Once the completed forms are returned to the Service, confirmation of receipt is sent to the claimant. The condensed form is then sent to the employer with a letter explaining that the Commissioner has received a claim alleging that the employee is due wages which were earned but not paid.

If the employer agrees that the claim is valid, the employer is instructed to forward a check to the Employment Standards Service, payable to the Division of Labor and Industry. If the employer asserts that the claim is invalid, the employer is instructed to provide an explanation and documentary evidence to support the employer's position. The employer is informed that in the event a reply is not received, an investigator will meet with the employer at a specified time and date to attempt to resolve the claim.

In approximately 20 percent of all Wage Payment and Collection cases, a check or other adequate response is received. In these instances, a decision is made without the necessity of a personal visit by an investigator. If a response is not received or is inadequate, a Wage and Hour Investigator visits the employer

at the scheduled date and time and attempts to resolve the claim. If agreement is reached, a check is collected for the claimant. If a claim cannot be resolved and the claim is determined to be valid, the case is sent to the Office of the Attorney General for appropriate legal action.

During 1984, a total of 2,128 claims were investigated. A total of 467 claims were filed for vacation pay or 22% of the total claims filed. Forty-three claims were filed for severance pay, or 2% of the total filed.

The informal, "let's get this dispute settled" method of resolving these claims results in speedy service to the claimant. A more structured approach as practiced by many Federal agencies would result in a long protracted period where the employee would be deprived of wages which are sorely needed. The great number of claims would necessitate a huge increase in the number of Federal Compliance Officers to investigate and resolve the claims. Many claims which are filed with this office are filed as a result of a referral from the Wage and Hour Division of the United States Department of Labor. There is no question but that the individual States are better able to serve the citizens in the collection of unpaid wages.

MONTANA

Montana's Wage Payment Act (Sections 39-3-201 Montana Codes Annotated through Section 39-3-215, MCA) provides one of the two alternatives a wage claimant may use to collect wages.

The other one would be to file a civil suit in court. In most cases court calendars are extremely burdened with cases and resolution is extremely slow.

When a wage claim is received in the office of the Labor Standards Division of the Montana Department of Labor and Industry, an investigation is commenced and a determination reached, if possible, of the validity of the claim.

In the event that either the claimant or respondent feels aggrieved by the determination, they have the right to a hearing. The hearing would be held under the Montana Administrative Procedure Act with rules of civil procedure and evidence applying.

If either party feels aggrieved by the decision of the hearing officer, the only appeal is to District Court for judicial review. The Labor Standards Division may apply to District Court for a judgment or an order enforcing the decision of the hearing officer or a default order. (See Section 39-3-212, MCA.)

Employers doing business in Montana are not required by law to provide vacation pay, but once promised or made part of the employment agreement that promise must be complied with. See Attorney General's Opinion No. 56, September 17, 1949. Once earned, the vacation pay cannot be withheld by the employer or

forfeited by the employee. Similarly, severance pay is not required by law to be given but meets the definition of wages once it's made part of the employment agreement.

In fiscal years 1982-1984, the Montana Department of Labor and Industry handled over 3,000 claims and collected over \$1,400,000 in wages and fringe benefits owed.

OKLAHOMA

Title 40 Oklahoma Statutes 1982 - Section 165.1(3) defines wages as follows:

"'Wages' means compensation owed by an employer to an employee for labor or services rendered, including salaries, commissions, holiday and vacation pay, overtime pay, severance or dismissal pay, bonuses and other similar advantages agreed upon between the employer and the employee, which are earned and due, or provided by the employer to his employees in an established policy, whether the amount is determined on a time, task, piece, commission or other basis of calculation."

Under Oklahoma Law, holiday pay, vacation pay, severance pay, dismissal pay, bonuses and other similar advantages agreed upon between the employer and the employee which are agreed on as an established policy are wages. (Emphasis added.)

Title 40, Oklahoma Statutes 1975, Section 165.11 defines the penalty for failure to pay wages or wage supplements:

"A. In addition to any other penalty or punishment otherwise prescribed by law, any employer who is a voluntary party to or subject to a bona fide written agreement to pay or provide benefits or wage supplements to employees or to a third party or fund for the benefit of employees and who willfully fails, neglects or refuses to pay the amount or amounts necessary to provide su

benefits or furnish such supplements within thirty (30) days after such payments are required to be made by law or by agreement, shall be guilty of a misdemeanor, and each such failure to make payment as required herein shall constitute a separate offense. Where such employer is a corporation, the president, secretary, treasurer or officers exercising corresponding functions shall each be guilty of a misdemeanor.

B. As used in this section, the term "benefits or wage supplements" includes, but is not limited to, reimbursement for expenses as agreed prior to contracting said expenses; health, welfare and retirement benefits; and vacation, separation or holiday pay."

Oklahoma's wage complaint procedures involves:

- (1) A letter apprising the employer of the wage complaint, reciting the law and the criminal remedy and ask that the employer respond or pay.
- (2) If after the 2nd notice to employer we feel the wages are due and owing based upon the facts, we ask the District Attorney to prosecute. Penalty for failure to pay wages is a misdemeanor -- punishment is up to a \$500.00 fine, one (1) year in the county jail, or both.

In 1983, the Oklahoma Department of Labor received 3,058 claims. During that same year, the Department collected approximately \$500,000 on 1,197 claims and referred to civil or criminal court an additional 1,147 claims involving more than \$1,000,000.

Vermont

In Vermont, when an employer has a written policy or other written agreement to pay its employees benefits or wage supplements, then, upon failure to pay such benefits, the employer becomes liable to its employees for actual damages and, in the

event of fraud, is subject to criminal prosecution. See Title 21, Vermont Statutes Annotated, Section 345a.

A terminated employee who has failed to receive severance pay pursuant to his employer's written policy or agreement may complain to the Wage and Hour Division of the Department of Labor and Industry for assistance. The Wage and Hour Division will investigate the claim and attempt to resolve it on an informal basis. Approximately two thirds of the complaints made to that division are resolved this way. If the unresolved complaint involves fraud, the Department of Labor and Industry will pursue criminal charges against the employer. If no fraud is involved, the employee is told of his right to sue for actual damages, and the Department's investigation file is made available for his use in the lawsuit.

Wisconsin

The Wisconsin Department of Industry, Labor and Human Relations enforces Chapter 109, Wisconsin Statutes, "Wage Payments, Claims and Collection." This chapter requires employer to pay to every employee, at least once per month or within 15 days after termination, all wages earned. For the purpose of Chapter 109, "wages" are defined to mean remuneration payable to an employee for personal services, including salaries, commissions, holiday and vacation pay, overtime pay, severance or dismissal pay, bonuses, and other similar advantages agreed upon

employer and the employee or provided by the employer to the employees as an established policy. The Department investigates and tries to adjust controversies between employers and employees as to alleged wage claims. If the Department finds wages are due and an employer refuses to pay, it may file a lawsuit against the employer when the employee has assigned his claim to the Department. Chapter 109 grants a lien to the Department upon the property of an employer for the full amount of any wage claim assigned to it. This lien is given precedence over all other debts, judgments, decrees, liens or mortgages against the employer. In a case where an employer fails to pay wages as required by Chapter 109, he is subject to both criminal penalties and increased liability of up to 50% of the wages owed. While precise statistics are not available, a significant portion of the wage claims investigated by the Department under Chapter 109 are severance pay claims.

IN THE UNITED STATES DISTRICT COURT
NORTHERN DISTRICT OF ILLINOIS
EASTERN DIVISION

NATIONAL METALCRAFTERS,
A DIVISION OF KEYSTONE
CONSOLIDATED INDUSTRIES,)
a Delaware corporation)

Plaintiff-)
Counterdefendant,)

v.)

No. 84 C 2190

DONALD J. MC NEIL,)
Superintendent, Wage)
Claims Division, Illinois)
Department of Labor,)

Defendant,)

Before the Honorable
George N. Leighton
U. S. District Court Judge

and)

BETTY JOHNSON, et al.,)

Intervenor-)
Defendants-)
Counterplaintiffs.)

Memorandum

This is a lawsuit seeking to enjoin the Illinois Department of Labor from commencing proceedings to enforce a determination made against plaintiff pursuant to state law. Specifically, the Department, through defendant McNeil, found that plaintiff violated Illinois law by willfully refusing to pay claimants (intervenor here) vacation pay due under collective bargaining agreements.

Exhibit H

The crux of plaintiff's cause of action is that Illinois law, as it relates to the vacation pay sought by intervenors, is pre-empted by the Employee Retirement Income Security Act (ERISA), 29 U.S.C. §1001 et seq., and by the National Labor Relations Act (NLRA), 29 U.S.C. §151 et seq. According to plaintiff, therefore, state court action or intervention to enforce the Department's demand for payment is improper. Defendant and intervenors, however, contend that federal pre-emption is inapplicable to what are essentially contract claims under collective bargaining agreements. In their view, a state court can fully adjudicate these claims.

The cause is before the court on the motions of plaintiff, defendant, and intervenors, pursuant to Fed.R.Civ.P. 56, for summary judgment on plaintiff's complaint. The parties do not dispute any material facts, and each moves for judgment as a matter of law, based on their pre-emption positions. Oral and written presentations having been submitted to the court, the only issue to be resolved is whether the Department's exercise of jurisdiction conflicts with any federal statute, specifically, whether it is pre-empted by either ERISA or the NLRA. That issue arises out of the

following facts.

I

Plaintiff, National Metalcrafters, a division of Keystone Consolidated Industries, a Delaware corporation with its principal place of business in Dallas, Texas, operates manufacturing facilities in Rockford, Illinois. Employees at plaintiff's Rockford plant traditionally have been represented by the International Union, United Automobile, Aerospace and Agricultural Implement Workers of America and its local Union No. 449 (the "Union"). Over the years the company and the Union entered into a number of consecutive collective bargaining agreements covering the employment terms of Union employees. The most recent agreement began on April 14, 1980, and expired on April 16, 1983. Section 6.1 of the agreement, entitled "Amount of Vacation & Vacation Pay," obligated the company to pay vacation benefits to Union employees based on length of service with the company.

Defendant Donald J. McNeil is Superintendent of the Wage Claims Division of the Illinois Department of Labor. He administers the provisions of the Illinois Wage Payment & Collection Act, Ill.Rev.Stat., ch.48 §39m-1, m-11 (the "Act"), a statute enacted to ensure that employers pay employees what is due under the terms of collective bargaining agreements. An employer who refuses to pay wages or final compensation earned under a Union contract violates the Act.

Prior to expiration of the 1980 bargaining agreement, plaintiff and the Union engaged in negotiations for a new agreement. As part of the new contract, plaintiff proposed a reduction in vacation benefits, the stated reason being to equalize Union employees' and salaried employees' vacation benefits. Plaintiff and the Union reached a bargaining impasse and when the 1980 agreement expired on April 16, 1983, the Union began a strike against the company which continues to the present day.

In May, 1983, the company unilaterally implemented the vacation benefits reduction plan, and in July, 1983, paid vacation benefits based on the new plan rather than under the 1980 agreement. Subsequently, the Union filed an unfair labor practice charge with

the National Labor Relations Board (NLRB) alleging that the company had violated the NLRA by, among other things, not paying vacation benefits as embodied in the terms of the 1980 agreement.^{1/} At about the same time, 150 Union employees brought claims before the Wage Claims Division of the Illinois Department of Labor, pursuant to the Act, for vacation wages earned and not paid by the company.

Following briefing and oral argument, defendant McNeill found that the company had withheld vacation pay from the employees in violation of the Act. He ordered it to pay claimants, within 15 days, the difference between the amounts of vacation pay actually given them in July, 1983, and the amounts they would have received had the benefits been calculated in accordance with the rates set forth in the 1980 contract between the company and the Union. In reaching his decision, defendant rejected plaintiff's arguments that the Act was pre-empted by ERISA and the NLRA, and found that he had jurisdiction over the claims. In defendant's view, ERISA did not pre-empt state intervention because the

^{1/} In March 1984, the Union withdrew, without prejudice, its charge on the vacations benefit issue.

vacation provisions of the Union contract under which claimants worked did not constitute an employee benefit plan within ERISA. "Indeed," defendant stated, "it does not appear that the company believed its vacation obligations were governed by ERISA, at least until it began preparing its defense to these claims...workers never have received ERISA-required reports." (Memorandum in Support of Demand for Payment, p. 8). Defendant also concluded that the NLRA pre-emption argument was without merit, because the case did not turn on an interpretation of federal labor law, but rather, on the provisions of the 1980 contract. Enforcement therefore would not "usurp the NLRB's authority...interfere with the collective bargaining process or dictate the outcome of ongoing negotiations." Id. at p. 7. In summary, defendant found that the company

[h]as wilfully refused to pay (vacation pay) as provided in the Wage Payment and Collection Act, and has falsely denied the validity of the instant claims, with intent to secure for itself an underpayment of its indebtedness to the claimants. A demand for payment will issue and the Department will take appropriate legal action to enforce said demand, absent voluntary compliance by the employer.

The company did not comply with defendant's Order.

Instead, it commenced this action seeking declaratory and injunctive relief to the effect that Illinois law, as it applied to the vacation pay claims, is pre-empted by ERISA and the NLRA. After the action was commenced, Betty Johnson, who was a claimant before defendant McNeil, intervened and filed counterclaims against plaintiff, on behalf of herself and all others similarly situated.

II

Congress enacted ERISA to protect working men and women from abuses in the administration and investment of private retirement plans and employee welfare plans. Donovan v. Dillingham, 688 F.2d 1367, 1370 (11th Cir. 1982). ERISA established certain minimum standards for the vesting of benefits, funding of benefits, carrying out fiduciary responsibilities, reporting to the government, and making disclosures to participants, id., so that "the private pension promise (would) become real, rather than illusory." H.R.Rep.No. 93-533, 93d Cong. 2d Sess., reprinted in 1974 U.S. Code Cong. & Ad. News 4639, 4648.

Title I of ERISA applies to any employee benefit

plan if it is established or maintained -

1) by any employer engaged in commerce or in any industry or activity affecting commerce; or

2) by any employee organization or organizations representing employees engaged in commerce or in any industry or activity affecting commerce; or

3) by both.

29 U.S.C. §1003(a).

An employee benefit plan can be either an "employee welfare benefit plan" or an "employee pension benefit plan" or a plan which is both. 29 U.S.C. §1002(3). An employee welfare benefit plan is described in the statute as

[a]ny plan, fund or program which was ...established or maintained by an employer...to the extent that such plan, fund, or program was established or is maintained for the purpose of providing for its participants or their beneficiaries... A)...benefits in the event of sickness, accident, disability, death or unemployment, or vacation benefits...

29 U.S.C. §1002(1).

ERISA contemplates that such plans shall be established pursuant to a written instrument providing for fiduciaries, and that the assets of the plan shall be held in trust by trustees to manage and control the assets of the plan. 29 U.S.C. §§1102, 1103.

Not all employee plans can meet these statutorily specific parameters. See 29 U.S.C. §1143(a)(1) ("there are types of plans not subject to this Act"). Additionally, the Secretary of Labor has enacted 29 CFR 2510.3-1 which exempts certain practices from ERISA coverage. These include:

Payment of compensation, out of the employer's general assets, on account of periods of time during which the employee, although physically and mentally able to perform his or her duties and not absent for medical reasons (such as pregnancy, a physical examination or psychiatric treatment) performs no duties; for example -

i) Payment of compensation while an employee is on vacation or absent on a holiday, including payment of premiums to induce employees to take vacations at a time favorable to the employer for business reasons.

29 C.F.R. 2510.3-1(b)(3)(i).

ERISA provides a broad pre-emption section. 29 U.S.C. §1144(a) states that

[t]he provisions of this title...shall supersede any and all state laws insofar as they may now or hereafter relate to any employee benefit plan described in Section 4(a)...

ERISA, however, does not pre-empt statutes regulating practices which either do not qualify as, or are excepted from the definition of, ERISA benefit plans, and therefore are not covered by the statute.

Shaw v. Delta Airlines, Inc., ___ U.S. ___, 103 S.Ct. 2890, 2903 (1983).

Plaintiff of course argues that its vacation pay plan was established pursuant to ERISA, and that Illinois law is pre-empted insofar as it relates to the plan. This court disagrees. The facts of this case simply do not substantiate plaintiff's claims. Here the court is pointed to no established fund, no beneficiaries and no fiduciaries. Plaintiff has submitted no evidence of a summary plan description, no annual reports, no trust agreement, which would lead the court to conclude that this was an ERISA fund established or maintained by the employer for the benefit of its employees. As noted by defendant McNeil, the ERISA pre-emption argument only seems to have come into play when plaintiff began preparing its defense to court actions instituted against it.

According to plaintiff, however, the "plain meaning" of the statute mandates a finding that its plan is within ERISA. While it is true that ERISA encompasses "vacation benefits" under the rubric of employee welfare plan, 29 U.S.C. §1002(1), it is equally true that such benefits must meet the other ERISA requirements that the assets of the plan be

funded in trust. The court does not dispute that in a proper case vacation benefits can fall within ERISA coverage, and be subject to federal pre-emption. See e.g., Baker v. Caravan Moving Corporation, 561 F.Supp. 337 (N.D.Ill. 1983). But this is not that case.

Plaintiff persists, however, and cites California Hospital Association v. Henning, 569 F.Supp. 1544 (C.D.Cal. 1983) as support for its view that all vacation plans and programs are covered by ERISA, "irrespective of whether such arrangement is funded, trustee, or embodied in a writing." Id. at 1546. Henning is a lone voice however, and it is in direct contravention of the statute. 29 U.S.C. §§1102, 1103. This court is of the opinion that Henning was wrongly decided, and that the better view is expressed in the interpretation of ERISA found in Taggart Corporation v. Life and Health Benefits Administration, Inc., 617 F.2d 1208 (5th Cir. 1980), cert. denied 450 U.S. 1030 (1981), where the court held that ERISA does not apply to a program with no assets, no fund, and no trust to be protected by ERISA.

Furthermore, Henning directly contradicts the Secretary's regulation exempting vacation benefits paid out of an employer's general assets from ERISA

coverage. The administrative interpretation of ERISA by those entrusted with its enforcement is entitled to great weight. Abella v. W.A. Foote Memorial Hospital, Inc., 740 F.2d 4 (6th Cir. 1984).

As this court stated to counsel at oral argument, the matter appears clear that the Act is not pre-empted by ERISA. ERISA has nothing to do with how collective bargaining agreements are administered or enforced. At issue here is whether a state agency can order an employer to pay wages earned under a collective bargaining agreement. That is a far cry from the purpose for which Congress enacted ERISA .

Even assuming arguendo, that plaintiff's vacation plan did fall within ERISA's provisions, ~~the~~ court doubts that plaintiff has standing to bring this action under ERISA. See 29 U.S.C. §1132(e)(1)(a civil action may only be brought by "the Secretary, or by a participant, beneficiary or fiduciary"). Also see Franchise Tax Board v. Construction Laborers Vacation Trust, ___ U.S. ___, 103 S.Ct. 2841 (1983). Nothing in the evidence or oral presentations made to this court indicates that plaintiff employer is either a participant, beneficiary, or fiduciary, and thus, entitled to bring an ERISA action.

A final factor in rejecting the ERISA pre-emption argument is that the Illinois law in question provides for criminal penalties. It has been held that any Act which sanctions criminal prosecution for failure to make certain wage payments is not pre-empted by ERISA. See 29 U.S.C. §1144(b)(4); Sasso v. Vachris, 116 Misc.2d 797, 456 N.Y.S.2d 629 (Sup. 1982). For the foregoing reasons, therefore, the court concludes that plaintiff's claim of ERISA pre-emption is without merit.

III

The court also rejects plaintiff's alternative argument of NLRA pre-emption. Not every state law dealing with terms and conditions of employment comes within the sweep of the federal labor laws. San Diego Building Trades v. Garmon, 359 U.S. 236, 243-44 (1959). To determine if state regulation is pre-empted by federal labor laws, a court must make a balanced inquiry into such factors as the nature of the federal and state interests and the potential for interference with federal regulation. State interests that are "a merely peripheral concern" of federal labor

law override the federal interest. Id. Alternatively, state regulation may escape pre-emption by being directed at state "interests so deeply rooted in local feeling and responsibility" that, in the absence of compelling congressional direction, (a court) could not infer that Congress had deprived the states of the power to act. Id. at 243, 244. See also, Gould Inc. v. Wisconsin Department of Industry, Labor and Human Relations, et al., Nos. 84-1115 and 84-2075, slip op. at 4-5 (7th Cir. December 13, 1984).

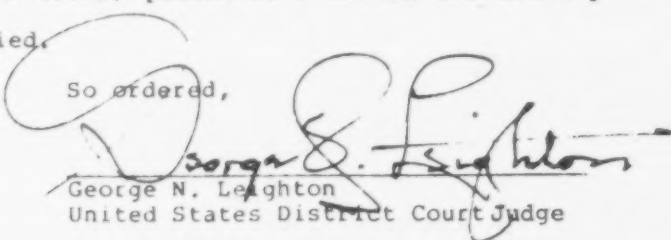
The Illinois Act is one that provides basic protections for the working citizens of Illinois. In balancing the interests at play here, it is plain to this court that the Department seeks to enforce rights which are "a merely peripheral concern" of federal law, and which implicate "interests so deeply rooted in local feeling and responsibility" that state action in no way interferes with the NLRB's authority.

IV

Summary judgment is appropriate in actions where there is no genuine issue of material fact, and the moving party is entitled to judgment as a matter of

law. Fed.R.Civ.P.56; Cedillo v. International Association of Bridge & Structural Iron Workers, 603 F.2d 7, 10 (7th Cir. 1979). The parties agree that there is no issue of material fact in dispute, and the court has carefully reviewed relevant law relating to pre-emption. The law is clear that the Illinois Wage Payment & Collection Act is not pre-empted by ERISA, or the NLRA, and the court concludes that defendant and intervenors are entitled to judgment as a matter of law. Accordingly, defendant's and intervenors' motions for summary judgment are granted, and judgment is entered in their favor; plaintiff's motion for summary judgment is denied.

So ordered,


George N. Leighton
United States District Court Judge

Dated: JAN 29 1985

Page 182a-5

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

-----X

IRVING GILBERT, et al., :

83 Civ. 6954-CLB

Plaintiff, :

and- :

LILLIAN ROBERTS, as Commissioner of :
Labor of the State of New York, :MEMORANDUM AND ORDER

Plaintiff-Intervenor, :

-against- :

BURLINGTON INDUSTRIES, INC., :

Defendant. :

-----X

Bricant, J.

In this action thirty-six former employees of the Sock and Hosiery Division of Burlington Industries, Inc. ("Burlington"), a major conglomerate, sue upon claims founded on the Employee Retirement Income Security Act of 1974 ("ERISA"), 29 U.S.C. § 1001, et seq., also pleading pendent contract, promissory estoppel, quantum meruit, and fraud claims as well as claims arising under statutes of New York and North Carolina said to be applicable, which relate to vacation and payroll severance benefits said to be due pursuant to a 1974 Burlington policy concerning severance pay.

In January 1982, Burlington sold to Kayser-Roth Hosiery, Inc. ("Kayser-Roth"), a large manufacturer, not a party to this litigation,

Exhibit I

all of its assets, trademarks, customer lists and goodwill used in and about its Sock and Hosiery Divisions. Under the sale agreement, Kayser-Roth agreed with Burlington "to use its best efforts to encourage all salaried and wage employees of the Operations, including all sales personnel to transfer to the employ of [Kayser-Roth]." (Plaintiff-Intervenor's Motion for Stay, filed March 12, 1984, Ex. H). The understanding between Burlington and Kayser-Roth that substantially all of the employees of the acquired Divisions would be retained is also set forth expressly in a supplemental agreement, dated December 18, 1981, which provides that, "[a]t the closing, [Kayser-Roth] will retain all employees, wage and salaried, of the Divisions . . .," except for five employees specifically referred to in the agreement. (Plaintiff-Intervenor's Motion for a Stay, Ex. G). Those five Burlington employees, not parties to this action, received severance benefits from Burlington.

After the sale, all of the plaintiffs, except one who retired, were employed by Kayser-Roth in the positions and at the salaries or rates of pay received previously from Burlington. However, plaintiffs here seek to enforce their rights to severance pay to the same effect as if Burlington had simply gone out of business with respect to its Sock and Hosiery Divisions, leaving them unemployed.

The Burlington policy regarding severance benefits, as set forth in the company Policy Manual as it existed at the time of sale of the Divisions to Kayser-Roth, provided in relevant part as follows:

"Section: Compensation - Salaried Employees

Sub-Sec: Terminations - Payroll Severance -
Vacation Severance

I. Company Policy

- A. General - The Company makes payroll severance payments and vacation severance payments to eligible salaried employees who are terminated from the Company.
- B. Payments - Payroll severance payments are based upon tables contained in this policy. Vacation severance payments are based upon a person's length of continuous service with the Company less vacation taken or adjusted as defined by this policy.

II. Application of Policy

- A. Payroll Severance - All regular full-time salaried employees who meet eligibility requirements are paid payroll severance based upon continuous service as shown in Exhibit A or Exhibit B.
 - 1. Eligibility - Employees are eligible to receive payroll severance if they are regular full-time salaried employees who are involuntarily terminated from the Company. Eligibility requirements are:
 - a. Job Elimination - This category consists of terminations due to circumstances such as elimination or modification of operations or other job elimination due to bona fide organizational changes.
 - b. Other Involuntary Terminations - These are terminations due to unsatisfactory job performance which is not willful.

* * *

2. Ineligibility - Employees are not eligible to receive payroll severance if:

a. Temporary Full-Time, Temporary Part-Time, or Regular Part-Time Employees - Employees assigned to these employment classifications are not eligible for payroll severance payments.

b. Ineligible Full-Time Employees - Employees who are terminated because of early retirement, mandatory retirement, death, misbehavior, lack of cooperation, willful negligence, or other unfriendly acts against the Company or towards its management are not eligible for payroll severance payments."

(Affidavit of Calvin A. Michaels, sworn to November 29, 1983, Exhibit A, at 1-2).

Defendant contends that this written policy applies only to employees who are involuntarily terminated and whose jobs are eliminated, leaving them unemployed, and that the use of the phrase "job elimination" evidences the intent to require the actual loss of a job as opposed to a mere termination from the Burlington payroll under circumstances which preserve the employee's job under new ownership and management of the same production assets. Plaintiffs argue that the plain, unambiguous language of the policy statement entitles them to severance pay.

●

Following the sale of the Divisions by Burlington, ten of the plaintiffs in this action filed claims with the New York State Department of Labor, pursuant to § 198-c of the New York Labor Law. Burlington applied to the New York State Commissioner of Labor ("the

Commissioner") to dismiss these claims, asserting that § 198-c is preempted by ERISA, and therefore the New York State Labor Department lacks jurisdiction to adjudicate the claims. On September 2, 1983, the Commissioner issued an Order to Comply with respect to plaintiff's claims. On September 8, 1983, Burlington appealed the Commissioner's decision to the Industrial Board of Appeals ("the Board"), again raising the preemption and jurisdictional issues, and was granted a stay of enforcement of the Order to Comply.

Prior to the issuance of the stay and on September 22, 1983, plaintiffs initiated this action alleging claims under ERISA and in the alternative under state law "because the case is governed either by state statutory and common law or by ... ERISA, but most probably not by both." (Complaint at ¶ 1). After the Board was informed of commencement of this action, it adjourned all further proceeding, but now indicates an intention to resume its adjudicatory process.

On December 12, 1983, Burlington moved to dismiss the plaintiffs' claims in this case, or, in the alternative, to grant it summary judgment.

On January 5, 1984, the Commissioner was granted leave to intervene in this action, and on February 3, 1984, Burlington counter-claimed against the Commissioner, alleging that:

"The New York State Department of Labor violated and continues to violate Section 114(a) of ERISA in (i) acting under Section 198-c of the New York Labor Law with respect to claims involving Burlington's severance benefit plan, (ii) assuming jurisdiction over such claims, (iii) issuing the Order to Comply, and (iv) failing to dismiss or discontinue all of the above described proceedings before it."

On March 16, 1984, the Commissioner moved to stay this federal action during the pendency of the state administrative proceedings. Thereafter, on April 13, 1984, Burlington requested that the Board adjourn its hearings since Burlington's motion was sub judice, and on April 20, 1984, the Board informed the parties that it intended to await this Court's determination of Burlington's motion before deciding whether to commence its own hearings.

In May, 1984, twenty-six additional claims for unpaid severance benefits were filed with the New York State Labor Department by former Burlington employees. All of these claimants are also plaintiffs in the instant action. Burlington responded as it had with respect to the earlier claims that they were preempted by ERISA.

Section 1144(a) of ERISA provides in pertinent part, that ERISA: "shall supersede any and all state laws insofar as they may now or hereafter relate to any employee benefit plan."

The central question raised by all of the pending motions is whether ERISA preempts plaintiffs' state statutory and common law claims.

As a threshold matter, this Court must determine whether Burlington's severance pay policy is an "employee benefit plan" within the coverage of ERISA. An "employee benefit plan" is defined as "an employee welfare benefit plan or an employee pension benefit plan or a plan which is both an employee welfare benefit plan and an employee pension benefit plan." 29 U.S.C. § 1002(3). The Burlington severance pay policy is clearly not an employee pension benefit plan, and therefore, it falls within the purview of ERISA only if it is an "employee welfare benefit plan." That term is defined to include:

"any plan, fund, or program which was heretofore or is hereafter established or maintained by an employer or by an employee organization, or by both, to the extent that such plan, fund, or program was established or is maintained for the purpose of providing for its participants or their beneficiaries, through the purchase of insurance or otherwise, (A) medical, surgical, or hospital care or benefits in the event of sickness, accident, disability, death or unemployment or vacation benefits, apprenticeship or other training programs, or day care centers, scholarship funds, or prepaid legal services, or (B) any benefit described in section 186(c) of this title (other than pensions on retirement or death, and insurance to provide such pensions)."
29 U.S.C. § 1002(1).

Defendant contends that since § 1002(1) includes "programs" which provide "unemployment" benefits, and since severance pay is among

the most common forms of unemployment benefits, it is clear that Congress intended to include severance pay plans as a form of employee benefit plan under ERISA. Burlington argues further that since the Act incorporates all of the types of benefits described in § 186(c) within the scope of the term "employee benefit plan," and since severance payments are specifically referred to in 29 U.S.C. § 186(c)(6), severance benefit plans are covered as employee benefit plans within the plain meaning of ERISA. Finally, defendant asserts that all federal courts heretofore addressing claims pursuant to severance pay plans have held that such benefits are covered by ERISA. See, e.g., Dhayer v. Weirton Steel Division of National Steel Corp., 571 F.Supp. 316, 320-30 (N.D.W.Va. 1983); Petrella v. NL Industries, Inc., 529 F.Supp. 1357 (D.N.J. 1982); Dependahl v. Falstaff Brewing Co., 491 F.Supp. 1188, 1196 (E.D. Mo. 1980), aff'd, 653 F.2d 1208 (8th Cir.), cert. denied sub nom. Dependahl v. Kalmarovitz, 454 U.S. 1084 (1981); Calhoun v. Falstaff Brewing Co., 478 F.Supp. 357, 359 (E.D. Mo. 1979); Donnelly v. Aetna Life Insurance Co., 465 F.Supp. 696, 698 (E.D. Pa. 1979); Pinto v. Zenith Radio Corp., 480 F.Supp. 361, 362-63 (N.D. Ill. 1979), aff'd, 618 F.2d 110 (7th Cir. 1980).

Plaintiffs argue that ERISA does not apply to Burlington's severance pay policy, and that therefore their state law claims need not be dismissed, because there is no plan as such, but simply a naked promise to pay severance benefits which is enforceable under state law. In support of their position, plaintiffs contend that every "employee

welfare benefit plan" must have an identity and structure of its own, evidenced by a written instrument naming a fiduciary, providing for a funding policy, allocating responsibilities among those who will administer the plan, establishing procedures for the plan, identifying persons with authority to amend the plan, and specifying the basis on which payments will be made to and from the plan. [Plaintiffs' Memorandum of Law, filed March 26, 1984, at 50, citing 29 U.S.C. §§ 1102(a) and (b)]. Plaintiffs also assert that a plan must either have identifiable assets of its own, independent from the general assets of the employer, or commit itself to establishing a funding policy that will assure that an adequate proportion of the employer's income will be dedicated to the plan. Finally, plaintiffs contend that to qualify as a severance pay employee benefit plan within the meaning of the Act, the plan must have been established as a Taft-Hartley Trust pursuant to § 302(c) of the Labor Management Relations Act, 29 U.S.C. § 186(c). Plaintiffs assert that Burlington's severance pay policy fails to satisfy any of these basic criteria.

This Court concludes, however, that the Burlington severance pay policy is an "employee welfare benefit plan" for the purposes of ERISA, and within the plain meaning of that statute. The existence of a "plan" under ERISA is to be determined solely by an examination of the Act's "coverage" and "definitional" sections. Donovan v. Dillingham, 688 F.2d 1367, 1372 (11th Cir. 1982) (*en banc*); Dependahl v. Falstaff Brewing Corp., *supra*. In construing the language used in a remedial

Congressional enactment, in the absence of absurdity, legislative history to the contrary, or some other compelling reason, a Court should conclude that the words used by Congress were meant to have their plain, normal and commonly accepted meaning. American Tobacco Co. v. Patterson, 456 U.S. 63, 68 (1982).

It is clear that the plain language of § 1002(1) encompasses severance pay plans such as the one set forth in Burlington's policy manual: it is a plan, established by an employer, for the purpose of providing an unemployment benefit to its participants, the Burlington employees, through the use of general corporate assets. See 29 U.S.C. § 1002(1)(A), and/or a benefit described, i.e., enumerated, in § 186(c) of Title 29.

Employee welfare benefit plans need not be funded in order to be within ERISA. See 29 U.S.C. §§ 1081 and 1082. Furthermore, plaintiffs misconstrue the import of the Act's fiduciary and reporting provisions: these provisions state the responsibilities of fiduciaries and administrators of plans covered by ERISA, but they do not set forth prerequisites for ERISA coverage. As the Court noted in Donovan, *supra*:

"because the policy of ERISA is to safeguard the well-being and security of working men and women and to apprise them of their rights and obligations under any employee benefit plan, ... it would be incongruous for persons establishing or maintaining informal or unwritten employee benefit plans ... to circumvent the Act merely because an

administrator ... failed to satisfy reporting or fiduciary standards." 688 F.2d at 1372.

Similarly, it would be incongruous to permit plaintiffs to undermine the express purpose of ERISA, the establishment of a uniform system under which employee benefits are defined and administered, by reason of defendant's alleged failure to comply fully with reporting requirements concerning a plan which meets the Act's basic criteria.

Moreover, the Court rejects plaintiffs' contention that an employee welfare benefit plan must have been established as a Taft-Hartley trust. The language of the Act simply refers to the types of benefits "described" in § 186(c), but does not require that such benefit plans meet all the criteria of Taft-Hartley trusts. See S.Rep. No. 127, 93rd Cong., 2d Sess. 3 reprinted in 1974 U.S. Code Cong. & Adm. News 4851 (genesis of subsection 1002(1)(B) is "[a]n amendment offered by Senator Javits extending coverage ... to all benefit arrangements described in or permitted by Section 302 of the Taft-Hartley Act") (emphasis added).

Finally, the regulations promulgated pursuant to ERISA contradict plaintiffs' assertion that in order to come within the Act, a severance pay arrangement must be funded by assets separate from the employer's general funds and that severance benefits to be paid from an employer's general assets are excluded from ERISA coverage. In an

interpretive bulletin explaining fiduciary responsibilities under the Act, the Department of Labor stated in question and answer form:

"Q: Must a welfare plan in which the benefits are paid out of the general assets of the employer have a procedure for establishing and carrying out a funding policy set forth in the plan instrument?

A: No. Section 402(b)(1) requires that the plan provide for such a procedure 'consistent with the objectives of the plan' and requirements of Title I of the Act. In situations in which a plan is unfunded and Title I of the Act does not require the plan to be funded, there is no need to provide for such a procedure. If the welfare plan were funded, a procedure consistent with the objectives of the plan would have to be established." 29 C.F.R. § 2509.75-5.

Similarly, in a statement accompanying a proposed amendment to ERISA regulations, the Department of Labor stated that:

"since the provision of severance pay is one of the recognized purposes for a welfare plan under section 3(1), it would seem that severance pay plans would in virtually all cases be welfare plans, whether or not they are also pension plans for the purposes of Title I of ERISA." 44 Fed. Reg. 11763 (1979).

Having determined that Burlington's severance pay policy is an "employee benefit plan" covered by ERISA, the Court will now address whether § 1144(a) preempts plaintiffs' state law claims.

Section 1144(a) of the Act states that ERISA supersedes any and all State laws "insofar as they relate to any employee benefit plan described in section 1003(a)" of the Act (emphasis added). This language has been construed broadly by the Supreme Court to preempt state

laws which "have a connection with or reference to "an employee benefit plan. Shaw v. Delta Airlines, Inc., ____ U.S. ____, 103 S.Ct. 2890 (1983).

Both § 198-c of the New York Labor Law and § 75-1.1 of the General Statutes of North Carolina, upon which plaintiffs rely in seeking severance payments "relate to" the Burlington severance pay plan. It follows that Congress has, by ERISA, preempted these state laws.

Accordingly, defendant is entitled to a final injunction and stay of enforcement of the Order to Comply, and of the pending proceedings before the New York State Industrial Board of Appeals and the New York State Commissioner of Labor on the ground of federal preemption. The Commissioner's motion to stay this action is denied. Defendant is also entitled to a final judgment dismissing all state law, non-ERISA claims, pleaded in this action. See, e.g., Dependahl v. Falstaff Brewing Corp., 491 F.Supp. 1188 (E.D. Mo. 1980), aff'd, 653 F.2d 1208 (8th Cir.), cert. denied sub nom. Dependahl v. Kalmanovitz, 454 U.S. 1084 (1981); Ogden v. Michigan Bell Telephone Co., 571 F.Supp. 520, 523-24 (E.D. Mich. 1983); Shaw v. Int'l Ass'n Machinists & Aerospace Workers Pension Plan, 563 F.Supp. 653, 658-59 (C.D. Cal. 1983).

. a matter of discretion, the Court denies so much of defendants' motion which seeks dismissal or summary judgment with respect to

the ERISA claims, with leave to renew when pre-trial discovery is complete.

There is no just cause for delay. Rule 54(b), F.R.Civ.P. A judgment shall enter dismissing the state claims and granting injunctive relief as set forth above. Counsel for the remaining parties shall confer and agree upon a scheduling order with respect to the ERISA claims. A status report conference will be held before the Court on November 27, 1984 at 9:30 A.M., or at an earlier date if counsel for either party so requests.

Settle a Rule 54(b) Judgment on five (5) days notice.

So Ordered.

Dated: New York, New York
September 17, 1984

CHARLES L. BRIEANT

Charles L. Brieant
U. S. D. J.

FILED

SEP 8 1983

IN THE UNITED STATES DISTRICT COURT
CENTRAL DISTRICT OF CALIFORNIA

CALIFORNIA HOTEL AND RESTAURANT ASSOCIATION,
a non-profit California corporation;
CALIFORNIA MANUFACTURERS ASSOCIATION, a non-profit California
corporation; CALIFORNIA MANUFACTURERS
ASSOCIATION, a non-profit California
corporation; CALIFORNIA MANUFACTURERS
ASSOCIATION, a non-profit California
corporation; CALIFORNIA MANUFACTURERS
ASSOCIATION, a non-profit California
corporation; CALIFORNIA HOTEL AND MOTEL
ASSOCIATION, a non-profit California
corporation;

No. CV 81-6659 PG(GK)

Plaintiffs,

ORDER

v.

(SUMMARY JUDGMENT)

PATRICK W. HENNING, Labor Commissioner,
Division of Labor Standards Enforcement,
Department of Industrial Relations,
State of California,

Defendants.

This action is before the court on cross-motions for summary judgment. There are no genuine issues of material fact, and summary judgment is appropriate for disposition of the matter.

Plaintiffs are trade associations who bring the action on behalf of themselves and their members. Both the associations and their members sponsor and administer vacation plans and programs for their employees. Defendant is the Labor Commissioner

[Signature]

of the State of California, whose Division of Labor Standards Enforcement issued, on September 30, 1982, internal Policy and Procedure Memorandum 82-4 ("the enforcement policy"), which has the effect of regulating the vacation plans and programs of plaintiffs and their members. Plaintiffs' chief contention is that this regulation is prohibited by principles of federal preemption invoked by the Employee Retirement Income Security Act of 1974, 29 U.S.C. §§ 1001, et seq. ("ERISA").^{1/}

1. EXTENT OF ERISA COVERAGE.

It is plaintiffs' position that all employee vacation plans and programs are covered by ERISA. Coverage of that statute is stated in Sec. 4:

Except as provided in subsection (b) and in sections 201, 301, and 401, this title shall apply to any employee benefit plan

Sec. 3(3) provides:

The term "employee benefit plan" or "plan" means an employee welfare benefit plan or an employee benefit plan or a plan which is both

"Employee welfare benefit plan" is, in turn, defined by Sec. 3(1)

as:

any plan, fund, or program which was heretofore or is hereafter established or maintained by an employer or by an employee organization, or by both, to the extent that such plan, fund, or program was established or is maintained for the purpose of providing for its participants or their beneficiaries, through the purchase of insurance or

otherwise. (A) medical, surgical or hospital care or benefits, or benefits in the event of sickness, accident, disability, death or unemployment, or vacation benefits, apprenticeship or other training programs, or day care centers, scholarship funds, or prepaid legal services, . . .

(Exhibits added.)

Accordingly, it would appear from the plain language of the statute that Congress intended ERISA coverage to embrace every plan or program of an employer engaged in activities affecting interstate commerce and established for the purposes of providing vacation benefits. Defendant disputes this conclusion.

Defendant first contends that the only welfare benefit plans subject to ERISA are formal plans funded by a trust, citing § 403 and Taspart Corp. v. Life & Health Benefits Adm. Inc., 617 F.2d 1208 (5th Cir. 1980). Section 403, however, only requires a trust if there are assets of a plan, as distinguished from a plan funded by an employer's general assets. With respect to Taspart, if it did in fact define employee welfare benefit plans by reference to trust funding -- a matter which is not entirely clear -- it is contrary to the statutory scheme and should be rejected in favor of the well-reasoned opinion in Donovan v. Billingham, 698 F.2d 1367 (11th Cir. 1982), which observed:

There is no requirement of a formal, written plan in either ERISA's coverage section . . . or its definitions section Once it is determined that ERISA covers a plan, the Act's fiduciary and reporting provisions do require the plan to be established pursuant to a written instrument . . . ; but clearly these are only the responsibilities of

administrators and fiduciaries of plans covered by ERISA and are not prerequisites to coverage under the Act.

Id. at 1372.

In short, by referring to § 401, et seq., of the Act, defendant is trying to back into the coverage result he desires. The process is illogical. If any of the vacation plans of plaintiffs or their members should be in writing or funded by trusts and are not, the issue thus presented is compliance, not coverage.

In arguing for restricted ERISA coverage of vacation plans defendant further relies on Department of Labor regulations promulgated shortly after ERISA's enactment. 29 C.F.R. § 2510.3-1 was designed to clarify the definition of "employee welfare benefit plan" and to identify certain practices which are not subject to Title I. Subsection 3-1(b) excludes from the definition of "employee welfare benefit plan" --

(1) Payment of compensation, out of the employer's general assets, on account of periods of time during which the employee, although physically able to perform his or her duties and not absent for medical reasons . . . performs no duties; for example --

(i) Payment of compensation while an employee is on vacation or absent on a holiday

Plaintiffs respond that this regulation does not exempt every vacation program in which benefits are paid from general assets of the employer and observe that such a construction would undoubtedly exempt the great majority of such programs. Rather,

1
2 they say, it applies only to those situations where there is an
3 employer's discretionary "practice" rather than a plan or pro-
4 gram to which the employer is committed, by contract or
5 otherwise. That is a sensible view of the regulation, since there
6 is a decided difference between the established plan or program
7 defined in Donovan, (i.e., (i) intended benefits, (ii) intended
8 beneficiaries, (iii) a source of financing and (iv) a procedure
9 for application and collection of benefits) and the situation
10 where an employer might on occasion simply tell a worker to take
11 a few days off. In support of their argument plaintiffs point to
12 a number of other regulations and Department of Labor Advisory
13 Opinions which apply Title I of ERISA to clearly unfunded pro-
14 grams.
15

16 It is not necessary to the decision in this case,
17 however, to adopt plaintiffs' construction of subsection 3-1(b)(3).
18 If that regulation does indeed intend ERISA exemption of every
19 unfunded vacation program, it is at clear odds with language of
20 the statute itself and an invalid arrogation of power by the
21 Department.

22 The conclusion is inescapable that any plan, fund, or pro-
23 gram, as those terms are defined by Donovan, maintained for
24 employee vacation benefits by an employer engaged in activities
25 affecting interstate commerce, is an employee welfare benefit
26 plan subject to ERISA coverage, irrespective of whether such
27 arrangement is funded, trusteeed, or embodied in a writing.
28

II. PREEMPTION OF STATE LAWS.

Federal preemption in this field is stated in ERISA

§ 514:

Sec. 514. (a) Except as provided in subsection (b) of this section, the provisions of this title and title IV shall supersede any and all state laws insofar as they may now or hereafter relate to any employee benefit plan described in section 4(a) and not exempt under section 4(b).

This provision has been aptly termed the most sweeping federal preemption statute ever enacted by Congress. Any doubt as to its ambit was recently put to rest by the Supreme Court in Shaw v. Delta Air Lines, Inc., 463 U.S. ___, 103 S.Ct. 2890, 76 L.Ed.2d ___ (1983). Also addressed by Shaw is the contention of defendant that state regulation is permissible in those areas not specifically covered by ERISA. The Court observed:

Nor, given the legislative history, can § 514(a) be interpreted to pre-empt only state laws dealing with the subject matters covered by ERISA -- reporting, disclosure, fiduciary responsibility, and the like. The bill that became ERISA originally contained a limited pre-emption clause, applicable only to state laws relating to the specific subjects covered by ERISA. The Conference Committee rejected these provisions in favor of the present language, and indicated that the section's pre-emptive scope was as broad as its language.

463 U.S. at _____. (Slip Opinion, p. 11.)

There can be no question but that the ERISA preemption provision prohibits all state regulation relating to employee welfare benefit plans.

111. THE STATE REGULATION HERE IN ISSUE.

The defendant's enforcement policy has its foundation in California Labor Code § 227.3, which provides in part that, when an employee is discharged without having used his vested vacation time " . . . all vested vacation shall be paid to him as wages at his final rate in accordance with . . . [the] employer policy respecting eligibility or time served" The section also prohibits forfeiture of vested vacation time on termination. In 1982 the Supreme Court of California confronted the question of when vacation time becomes "vested." Suastez v. Plastic Dress-Up Co., 31 Cal.3d 774. Construing § 227.3, a unanimous Court held that vacation benefits vest as labor is rendered and that an employee, on termination, must be paid -- as wages -- his prorata share of such benefits. The opinion did not discuss the issue of ERISA preemption, which was first raised in a petition for rehearing. Defendant's enforcement policy, which sets out guidelines for administering employee claims in light of Suastez, followed the denial of rehearing by a few days.

It is obvious that the enforcement policy is a state law within the meaning of § 514, as are also Labor Code § 227.3 and Suastez, to the extent that they relate to employee welfare benefit plans. Subsection (c) of § 514 provides:

the term "state law" includes all laws, decisions, rules, regulations, or other state action having the effect of law, of any state.

As the Court in *Idaw* observed:

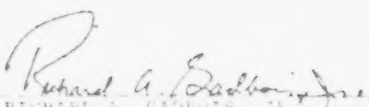
A law "related to" an employee benefit plan in the normal sense of the phrase, if it has a connection with or reference to such a plan.

463 U.S. at ____ (Slip Opinion, p. 10.)

The enforcement policy clearly "relates to" any California vacation plan since it directly regulates participation, vesting and benefit calculations.

This court accordingly concludes that defendant's enforcement policy, insofar as it purports to regulate those vacation plans of plaintiffs and their pool in which are in fact employee welfare benefit plans under ERISA, is an invalid assertion of state authority in an area which Congress specifically intended federal regulation to preempt.

Judgment is ordered for plaintiffs. Since the case is determined by ERISA preemption it is not necessary to address plaintiffs' alternative contentions.


 RICHARD A. GAGNOIS, JR.
 United States District Judge

DATED: SEP 8 1993

FOOTNOTES

1/ Further references to ERISA will employ numeration of the Act itself, rather than that of the United States Code.

2/ E.g., 39 C.F.R. 2535.104-20(b)(2)(i), and Advisory Opinions 81-55A, 75-128, 78-3A.

THE UNITED STATES DISTRICT COURT
FOR THE MIDDLE DISTRICT OF NORTH CAROLINA
GREENSBORO DIVISION

JOHN W. BARNETT, et al.

Plaintiffs, v.

BURLINGTON INDUSTRIES, INC., et al.

Defendants.

Case No. 274-G

MEMORANDUM OF DECISION

ERWIN, District Judge.

This cause came on for hearing on August 27, 1984 at the United States Courthouse in Greensboro upon motions filed by all parties in the case. Plaintiffs are 202 former employees of defendant Burlington Industries, Inc., (Burlington) Sock and Hosiery Division. The case centers on whether plaintiffs are entitled to benefits under a severance pay policy in effect at the time defendant Burlington sold its Sock and Hosiery Divisions to Kayser-Roth Corporation in 1982 as ongoing concerns. After defendant Burlington refused to pay any benefits under the severance policy to its former employees who now work for Kayser-Roth, plaintiffs filed an action in state court alleging five grounds for relief. All five grounds are based on state statutory and common law. The first ground alleges common law breach of contract. The second ground alleges violation of N.C. Gen Stat. 6-65-25.7, which requires employers to pay employees all wages

Exhibit K

due at the time of termination of employment. The third ground is based on the theory of equitable estoppel. The fourth ground is based on the contract theory of reliance. The fifth ground alleges violation of N.C. Gen. Stat. § 75-1.1, which prohibits unfair or deceptive trade practices.

Thereafter, defendant Burlington petitioned for removal of the action to federal court, asserting that the severance pay policy is an employee benefit plan subject to the Employment Retirement Income Security Act (ERISA), 29 U.S.C. § 1001 et seq. Without prejudging in any fashion the merits of the intervenor complaint, this court allowed the North Carolina Commissioner of Labor to intervene in the federal action.

In federal court, plaintiffs filed a motion for preliminary injunction to enjoin defendant Burlington from refusing to consider any of the plaintiffs for re-employment with Burlington so long as they were plaintiffs in the present action. Plaintiffs were then granted leave to file an amended complaint which added three new defendants, all executives of defendant Burlington, and which alleged three additional grounds for relief. The three grounds for relief are based on federal statutory law. The sixth ground for relief alleges that plaintiffs are entitled to benefits under the severance pay policy pursuant to 29 U.S.C. § 1132(a)(1)(B). The seventh ground alleges that defendant's refusal to consider any of the plaintiffs for re-employment constituted discrimination in violation of 29 U.S.C. § 1140. The eighth ground alleges that the three new defendants breached

their fiduciary duty with respect to the severance pay policy as defined in 29 U.S.C. § 1104(a)(1).

Defendant Burlington then filed a motion for summary judgment pursuant to Rule 56, F.R.Civ.P., against plaintiffs and plaintiff-intervenor with supporting brief, affidavits, and depositions. Thereafter, plaintiffs filed a motion for partial summary judgment on the three claims based on ERISA pursuant to Rule 56, F.R.Civ.P., with supporting brief, affidavits, and depositions. Additionally, plaintiff-intervenor filed a motion to dismiss for lack of federal jurisdiction, alleging that Burlington's severance pay policy is not governed by ERISA.

Plaintiff-Intervenor's Motion to Dismiss

In its motion to dismiss, plaintiff-intervenor contends that defendant Burlington's severance pay policy is not governed by ERISA; therefore, there is no basis for federal jurisdiction. Furthermore, plaintiff-intervenor asserts that defendant Burlington failed to allege any alternate grounds for federal jurisdiction and moves for a remand of this action to the state courts. The issue before the court is whether defendant Burlington's severance pay policy is governed by ERISA. The thrust of plaintiff-intervenor's argument is that defendant's severance pay policy is a payroll practice policy subject to the North Carolina Wage and Hour Act rather than an employee welfare benefit plan subject to ERISA. In support of its argument, plaintiff-intervenor contends that:

1. Defendant's severance pay policy does not satisfy the required statutory scheme because it is funded from Burlington's

general assets and does not have a separate entity from defendant;

2. The Department of Labor has exceeded its authority where it appears to expand the definition of employee welfare benefit plans to include all severance pay arrangements, even where they are not set as jointly administered trust funds; and

3. Defendant has failed to comply with ERISA's formal requirements regarding an employee benefit plan and should be estopped from using ERISA as a shield to avoid liability under the North Carolina Wage and Hour Act.

All of these contentions are without merit. First, both the statute and case law include severance pay arrangements within the definition of employee welfare benefit plans for purposes of ERISA coverage. Title 29 of the United States Code, Section 1002(2)(B), states: "The Secretary may by regulation prescribe rules consistent with the standards and purposes of this chapter providing one or more exempt categories under which . . . severance pay arrangements . . . shall, for purposes of this subchapter, be treated as welfare plans rather than pension plans." The Secretary has promulgated such a rule which treats a severance pay plan as an employee welfare benefit plan. 29 C.F.R. § 2510.3-1(a)(3) (1983). Additionally, the courts have consistently held that severance pay plans were employee welfare benefit plans under ERISA. See Sly v. P. R. Mallory & Co., Inc., 712 F.2d 1209 (7th Cir. 1983); Dhayer v. Weirton Steel Division of National Steel Corp., 571 F. Supp. 316 (N.D. W.Va. 1983); Donnelly v. Aetna Life Ins. Co., 465 F. Supp. 696, 698 (E.D. Pa.

1979); Calhoun v. Falstaff Brewing Corp., 478 F. Supp. 357, 359 (E.D. Mo. 1979); Petrella v. NL Industries, Inc., 529 F. Supp. 1357 (D.N.J. 1982); Pinto v. Zenith Radio Corp., 480 F. Supp. 361, 362-63 (N.D. Ill. 1979), aff'd, 618 F.2d 110 (7th Cir. 1980); Dependahl v. Falstaff Brewing Corp., 653 F.2d 1208 (8th Cir.), cert. denied sub nom. Dependahl v. Kalmanovitz, 454 U.S. 1084 (1981).

Secondly, there is no case law to support the proposition that severance pay arrangements must be funded from trust assets separate from the employer's general assets or that the arrangement must exist as a separate entity. As the court in Dhayer v. Weirton Steel Division of National Steel Corp., supra, at 330, noted: "Indeed, the funding requirements of ERISA do not apply to employee welfare benefits plans such as a severance pay benefit, 29 U.S.C. § 1081, and there is no 'fund' or group of assets subject to the prohibited transaction provisions."

Lastly, plaintiff-intervenor's equitable estoppel argument does violence to the purpose of ERISA. The court in Donovan v. Dillingham, 688 F.2d 1367, 1372 (11th Cir. 1982), aptly observed:

[B]ecause the policy of ERISA is to safeguard the well-being and security of working men and women and to apprise them of their rights and obligations under any employee benefit plan . . . it would be incongruous for persons establishing or maintaining informal or unwritten employee benefit plans, or assuming the responsibility of safeguarding plan assets, to circumvent the Act merely because an administrator or other fiduciary failed to satisfy reporting or fiduciary standards.

Therefore, the court finds that defendant Burlington's severance pay policy is governed by ERISA, and the court has jurisdiction of this case. Accordingly, plaintiff-intervenor's motion to dismiss must be denied.

Defendant Burlington's Motion for Summary Judgment

In its motion for summary judgment, defendant Burlington contends that plaintiffs and plaintiff-intervenor's claims based upon state laws are preempted by federal law and that defendant should prevail as a matter of law on the remaining claims based on ERISA. The court will first address the effect of preemption on the state law claims asserted by plaintiffs and plaintiff-intervenor.

Federal Preemption of State Law Claims Under ERISA

The Employment Retirement Income Security Act of 1974 regulates employee fringe benefit plans. ERISA provides for preemption of state law in 29 U.S.C. § 1144(a) as follows:

(a) Except as provided in subsection (b) of this section, the provisions of this subchapter and subchapter III of this chapter shall supersede any and all State laws insofar as they may now or hereafter relate to any employee benefit plan described in section 1003(a) of this title and not exempt under section 1003(b) of this title. This section shall take effect on January 1, 1975.

Although specific kinds of state laws are exempt from preemption under this statute, see 29 U.S.C. § 1144(b)(2)(A), the effect of the preemption provision is quite broad. Relying on the legislative history of the statute as well as the statute's plain language, the Supreme Court in Shaw v. Delta Air Lines, Inc., ____ U.S. ____ 51 U.S.L.W. 4968 (June 24, 1983), held that 29 U.S.C. § 1144(a) could not be interpreted to preempt only state laws dealing with specific subject matters covered by ERISA but preempted state laws that "relate to any employee benefit plan" within the meaning of the statute. Thus, it is clear that state

laws (including all laws, decisions, rules, regulations, or other state action having the effect of law) are preempted by ERISA if they "relate to" employee benefit plans not exempted by the statute.

In his complaint, plaintiff-intervenor alleges that the defendant Burlington is liable to the individual plaintiffs for severance pay pursuant to the North Carolina Wage and Hour Act, N.C. Gen. Stat. § 95-25.1 et seq. Wages are defined by the Act as specifically including severance pay. N.C. Gen. Stat. § 95-25.2(16). The Act also allows either employees or the Commissioner of Labor to bring a civil action to recover unpaid wages and provides for exemplary damages and injunctive relief.

The court has held that Burlington's severance pay plan is an employee benefit plan subject to ERISA. Inasmuch as the North Carolina Wage and Hour Act defines severance pay as wages, the state statute "relates to" the severance pay plan of Burlington. Accordingly, plaintiff-intervenor's claims under the Act are preempted by ERISA. Therefore, the court must grant defendant's motion for summary judgment as to the claims asserted by the plaintiff-intervenor.

Plaintiffs' second claim for relief is also brought pursuant to the North Carolina Wage and Hour Act. For the reasons stated above, the court must grant defendant's motion for summary judgment with respect to plaintiffs' second claim for relief.

In their first, third, and fourth claims for relief, plaintiffs allege they are entitled to recover severance pay based on common law contract and estoppel theories. These common law

claims "relate to" defendant Burlington's severance pay plan and are preempted by ERISA under 29 U.S.C. § 1144(a). Therefore, the defendant Burlington's motion for summary judgment as to plaintiffs' first, third, and fourth claims must be granted.

Plaintiffs' fifth claim based on the North Carolina Unfair Competition Act, N.C. Gen. Stat. § 75-1.1 must be dismissed because the provisions of the Act do not apply to employer-employee relationships. Buie v. Daniel Intern Corp., 56 N.C. App. 445, 289 S.E.2d 118 (1982). Therefore, defendant's motion for summary judgment with respect to plaintiffs' fifth claim must be granted.

Claims Based upon ERISA

A careful review of the record indicates that there is no genuine issue of material fact and that defendants are entitled to judgment in their favor as a matter of law on the remaining claims based upon ERISA. The standard of review of a claims decision made by a plan administrator is whether the administrator's decision was arbitrary or capricious. Horn v. Mullins, 650 F.2d 35 (4th Cir. 1981). This standard of review is applied whether the "plan" is an employee pension plan or, as here, an employee welfare benefit plan providing for severance pay. Sly v. P. R. Mallory & Co., 712 F.2d 1209, 1211 (7th Cir. 1983). Thus, the court must determine whether there is substantial evidence to support defendants' decision to deny severance pay to plaintiffs.

Plaintiffs contend that the governing document in this case is the Salaried Employees Handbook. The handbook contains highlights of Burlington's benefit plans. The handbook is distributed

to all salaried employees of Burlington and contains a description of the defendant Burlington's severance pay plan. The court finds, however, that the governing document for the administration of the severance pay plan is the Company Policy Manual rather than the Salaried Employees Handbook. The Policy Manual contains a compilation of formal policy statements. Although the salaried employees were not provided with a copy of the policy manual, the employees did have access to it.

The Policy Manual contained a section dealing with severance pay as early as June 1953. The provisions of that section were revised on various occasions during the relevant period. A 1974 revision provided that "job elimination" was a condition of eligibility for severance pay. The language in effect at the time of the sale of the Sock and Hosiery Divisions to Kayser-Roth provided in pertinent part:

1. Eligibility- Employees are eligible to receive payroll severance if they are regular full-time salaried employees who are involuntarily terminated from the Company. Eligibility requirements are:
 - a. Job Elimination - This category consists of terminations due to circumstances such as elimination or modification of operations or other job elimination due to bona fide organizational changes.

Plaintiffs argue that "job elimination" applies to involuntary terminations of employees when their jobs are eliminated with defendant, regardless of the availability of employment elsewhere. Defendants, on the other hand, argue that the words, "job elimination" refer to the elimination of jobs as such and that when jobs are preserved as a result of an organizational change, the mere loss of employment at Burlington

does not trigger eligibility for severance pay. The court finds that defendants' interpretation of its plan is rational in view of the plain language of the plan, the purpose of the plan, and defendants' past practices in relation to the severance pay plan.

Burlington established its severance policy for the purpose of providing financial support to employees whose jobs are lost through no willful fault of their own and who might therefore be in need of financial resources during a period of unemployment. It is evident that since the inception of Burlington's present severance policy in 1974, defendants have consistently applied that policy in the context of plant and division sales to bar severance pay to employees who continue in their jobs under new management. The court notes that a payment to Fleet Services employees who were terminated by Burlington but who continued working with new employers was a special cash award rather than severance pay. The court finds that defendants' decision to deny plaintiffs severance pay benefits was supported by substantial evidence on the record and was not arbitrary or capricious.

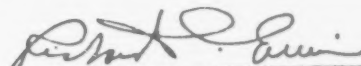
In their seventh claim for relief, plaintiffs allege that defendants have discriminated against them by refusing to consider plaintiffs for re-employment with Burlington because they filed this lawsuit. Plaintiffs seek injunctive relief. Title 29 of the United States Code, Section 1140, prohibits discrimination against a participant for exercising any right to which he is entitled under ERISA or under the employee benefit plan or for the purpose of interfering with the attainment of any right to which the participant may become entitled under the plan.

The court finds that plaintiffs' seventh claim is moot. Although the deposition of Burlington's director of personnel reveals that defendants adopted a policy after this action was filed of refusing to consider the plaintiffs for re-employment, this policy was subsequently revoked. Quintana's Affidavit. There is no evidence that at the present time, plaintiffs who seek re-employment with Burlington are being denied consideration. Therefore, the court finds that injunctive relief is inappropriate.

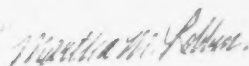
Plaintiffs' eighth and final claim for relief alleges that Burlington and three employees of Burlington who hold management responsibility for the personnel policies of Burlington breached fiduciary duties owed to plaintiffs under ERISA. This claim is without merit. As the court noted previously, defendants' decision to deny plaintiffs severance pay is supported by substantial evidence on the record and was not arbitrary or capricious. Therefore, the court finds that defendants discharged their duties in administering the severance pay plan with diligence and prudence and in accordance with the documents governing the plan. 29 U.S.C. § 1104(a)(1).

For the foregoing reasons, IT IS ORDERED, ADJUDGED, AND DECREED that defendants' motion for summary judgment is hereby GRANTED; that plaintiffs' motion for partial summary judgment is hereby DENIED; and that plaintiff-intervenor's motion to dismiss is hereby DENIED. IT IS FURTHER ORDERED, ADJUDGED, AND DECREED that plaintiffs' motion for preliminary injunction is hereby

DENIED. A judgment will be entered contemporaneously with this Memorandum Opinion dismissing this action with prejudice as to the defendants.


United States District Judge

October 17, 1984





Older Women's League

NATIONAL OFFICE

1325 G Street, N.W., Lower Level B, Washington, DC 20005
(202) 783-6686

June 4, 1985

Chairman William Clay
Subcommittee on Labor-Management Relations
Committee on Education and Labor
2451 Rayburn House Office Building
Washington, D.C. 20515

Dear Chairman Clay:

On behalf of the Older Women's League, I am submitting the attached comments on H.R. 2110 for inclusion in the Subcommittee compilation of comments.

Thank you for your continued efforts to enact fair pension reform and for inviting our comments. We know you will do all you can to make sure that the essential substance and intent of the Retirement Equity Act remain intact.

Sincerely,

Victoria Jaycox
Victoria Jaycox
Executive Director

COMMENTS ON H.R. 2110
from the
OLDER WOMEN'S LEAGUE
to the
SUBCOMMITTEE ON LABOR-MANAGEMENT RELATIONS

June, 1985

The Older Women's League (OWL) is a national membership organization representing the special concerns of women in their middle and later years. The nearly 14,000 members of OWL have selected pension equity as one of the priority issues for OWL's national agenda. Last year's passage of the Retirement Equity Act (REA) is hailed by OWL as a victory for women -- and men -- because of the progress it represents toward a fairer system of retirement income.

As advocates of REA from its early stages on through enactment, OWL continues to support the principles of, and approach to, pension equity embodied by REA. This legislation has helped improve pension receipt by women workers and spouses, and will continue to benefit more in the future. We are aware that there are persons who favor a reversal of REA provisions. OWL stands firmly opposed to any provisions that reverse the original intent of REA through the avenue of technical corrections.

OWL supports the clarifications and corrections made by H.R. 2110 with one exception. This is the provision in the section on coordination with qualified plan requirements, which prevents the distribution of benefits over \$3,500 in carrying out a qualified domestic relations order prior to the date of the participant's termination or attainment of early retirement age. Such payment is declared in violation of Internal Revenue Code requirements by H.R. 2110. This change represents a loss in fairness for women as well as for men because it denies the delivery of benefits to rightful payee when it may be needed most. OWL supports the original standing of REA on this matter.

FINLEY KUMBLE WAGNER HEINE UNDERBERG MANLEY & CASEY

1120 CONNECTICUT AVENUE, N.W.
WASHINGTON, D.C. 20036TEL: (202) 462-1000
CABLE: FINLEYTELEX: 880000, WHEWILL
TELETYPE: 880000 WHEWILLNEW YORK OFFICE
NEW YORK, N.Y. 10020
(212) 477-1000SAN FRANCISCO OFFICE
SAN FRANCISCO, CALIF. 94104
(415) 774-1000LOS ANGELES OFFICE
LOS ANGELES, CALIF. 90017
(213) 477-1000CHICAGO OFFICE
CHICAGO, ILL. 60601
(312) 477-10001000 K STREET, N.W.
SUITE 200
WASHINGTON, D.C. 20004
(202) 462-10001000 K STREET, N.W.
SUITE 200
WASHINGTON, D.C. 20004
(202) 462-10001000 K STREET, N.W.
SUITE 200
WASHINGTON, D.C. 20004
(202) 462-1000

(202) 857-4563

June 12, 1985

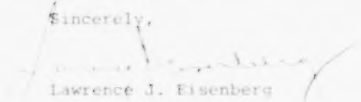
HAND DELIVERY

Ms. Phyllis Borzi
Pension Counsel
House Subcommittee on Labor-
Management Relations
2451 Rayburn House Office Building
Washington, D.C. 20515

Dear Ms. Borzi:

On behalf of the Small Business Council of America, Inc., I am pleased to submit for consideration of the House Subcommittee on Labor-Management Relations our testimony regarding technical corrections to the Retirement Equity Act of 1984. Five copies are enclosed.

Sincerely,


Lawrence J. Eisenberg

Enclosures

cc: Morton A. Harris, Esquire
Louis H. Diamond, Esquire

STATEMENT OF
SMALL BUSINESS COUNCIL OF
AMERICA, INC.

commenting on

PROPOSED TECHNICAL CORRECTIONS
to the
RETIREMENT EQUITY ACT OF 1984

TO BE ADDED TO THE RECORD OF THE HEARINGS ON H.R. 2110,
TO MAKE TECHNICAL CORRECTIONS TO THE RETIREMENT EQUITY
ACT OF 1984.

Morton A. Harris, Esquire
Louis H. Diamond, Esquire
Lawrence J. Eisenberg, Esquire

STATEMENT OF SMALL BUSINESS COUNCIL OF AMERICA, INC.

PROPOSED TECHNICAL CORRECTIONS TO THE
RETIREMENT/EQUITY ACT OF 1984INDEX

	<u>Page</u>
I. INTRODUCTION	1
II. SURVIVOR ANNUITY REQUIREMENTS	2
A. Spousal Consent Requirements for Survivor Annuities	2
1. Informed Consent Clarification	3
2. Option of "One-Time" Spousal Consent	5
3. Possible Conflict with State Law	6
4. Right of Spouse to Consent at Any Time	6
5. Clarify that Spousal Consent is Not the Transfer of a Property Interest	7
6. Conflict with Prenuptial Contracts	8
B. Qualified Preretirement Survivor Annuity Clarification	9
C. Clarification of Notification for Employees Hired After Age 35	10
D. Clarification of Impact of Fully Funded Survivor Annuities on Waiver, Consent and Notice Requirements under Code Section 417	11
E. Clarification of Exclusion of Voluntary Contributions	12
III. SPOUSAL CONSENT REQUIREMENTS - EXPANSION TO PLAN LOANS	13
A. Practical effects of Act Section 2(b)(4) - Recommendation	13
B. Suggested Clarifying Amendments	18
C. Remaining Technical Issues	18
IV. TRANSFEREE PLAN RULES	19
V. SEP ELIGIBILITY	21
VI. LUMP SUM TREATMENT; RECAPTURE OF TAXES	22

On behalf of the Small Business Council of America, Inc. we appreciate very much the opportunity to provide this statement for consideration by the House of Representatives Committee on Education and Labor, the Committee on Ways and Means, and the Senate Finance Committee, regarding the H.R. 2110, Proposed Technical Corrections to the Retirement Equity Act (the "Act").

I Introduction

The Small Business Council of America, Inc. ("SBCA") is a non-profit corporation which represents the interests of over 2,000 small business organizations located in 49 states. Most of these businesses maintain employee benefit plans qualified under Section 401(a) of the Internal Revenue Code. Consequently, SBCA represents the interests of a great number of businesses (and therefore employees) across the country who have a significant stake in legislation which affects the operational nature of qualified plans.

The Retirement Equity Act of 1984 ("REA") is perhaps the most complex tax act affecting pension plans since the Employee Retirement Income Security Act of 1974 ("ERISA"); and, in addition, REA has created many unanswered questions regarding the operation and administration of qualified plans. To date the Internal Revenue Service has provided little guidance as to the application of the REA provisions.

- 2 -

While we appreciate efforts made by Congress to eliminate uncertainties which exist under the provisions of REA as enacted, nevertheless, we believe that the proposed Act does not address all of the problems brought on by REA, and even creates areas of additional concern. This Statement, however, will be limited to matters that are appropriate within the scope of the Act, and to the extent feasible, the Statement will propose solutions.

II. Survivor Annuity Requirements

A. Spousal Consent Requirements for Survivor Annuities

Act Section 2(b)(6) clarifies the spousal consent requirement necessary for an employee to waive a qualified joint and survivor annuity and a qualified preretirement survivor annuity. Under REA, the spouse's consent must acknowledge the "effect" of the election in order for the employee to waive either of the survivor annuities. Code Section 417(a)(2). The Act clarifies this provision to specifically require designation of the beneficiary to whom the entitlements are to be paid, which may not be changed without the spouse's consent. The Act also provides a "one-time" consent by the spouse which permits the employee to designate (or redesignate) beneficiaries at any time without the spouse's further consent.

- 3 -

1. Informed Consent Clarification

SBCA commends the clarification of the spousal consent requirement. REA as currently enacted is too vague as to what information must be provided in order to properly obtain a spouse's informed consent to waive the survivor annuities. This problem is exacerbated by a lack of guidance in the Code, regulations, or by the Internal Revenue Service. As a result of this uncertainty there is extreme exposure, especially to small businesses, of plan litigation due to a failure to provide "informed" consent to the spouse. Moreover, as it now stands, REA subjects attorneys, accountants, administrators, and other plan advisers to an unprecedented exposure to malpractice lawsuits should a spouse believe she was not adequately informed of her rights. The Act, by clarifying the scope of the consent to specifically require naming the beneficiary, is a step in the right direction towards clarifying what constitutes informed consent.

SBCA strongly recommends that additional guidance be provided as to what "effects" have to be described to suffice as the consent requirement. Given the above risks, notices and consents provided by plan administrators and attorneys have tended to err on the side of providing as much information as possible, even though this is very burdensome to administrators and participants alike. The complexities of the notices and consents have frustrated everyone. To illustrate, a conservative interpretation of REA would require that the

- 4 -

spousal notice and consent provide a comparison of the actual benefits payable under the plan under the various options. (This requirement existed under the survivor annuity rules under Code Section 401(a)(11) prior to the enactment of REA). This can result in staggering actuarial costs, especially since the notice and consent would have to be provided each time the employee changes his beneficiary.

To eliminate uncertainty, minimize administrative costs, and decrease the risk of lawsuits, SBCA strongly urges that Congress mandate the Internal Revenue Service to provide "sample" written notices and consents which would satisfy the informational requirements necessary for proper spousal consent. We would also suggest that these notices not require that the actual amount of benefits payable under the distribution methods provided by the plan be stated. This will help minimize the actuarial costs of providing these notices. Alternatively, SBCA urges that Congress mandate the Treasury to provide, as soon as possible, "safe-harbor" regulations which spell out precisely what information is required in order to properly inform a spouse of his or her rights under REA. Either the sample consent or the safe harbor regulations would significantly benefit the consenting spouse, as well as decrease expenses and the exposure of small businesses to plan litigation. These improvements would well be worth the cost of amending forms and incurring additional legal costs,

- 5 -

consequences which would almost certainly follow passage of this Act.

2. Option of "One-Time" Spousal Consent

SBCA also approves the "one-time" spousal consent as a means to simplifying the onerous consent requirements now pertaining to the waiver of survivor annuities. SBCA recognizes that some feel that this provision is an "undoing" of REA, in that the "one-time" spousal consent does not protect the spouse should financial circumstances change, or the relationship with the beneficiary is altered. (Information derived from speech by William M. Leiber, Pension Counsel to the Joint Committee on Taxation, at the American Law Institute - American Bar Association Conference, Washington, D.C., April 25, 1985.) We believe, however, that this problem may be minimized by regulations or rulings promulgated by the Internal Revenue Service, and urge their immediate promulgation or issuance should this Act take effect. All things considered, SBCA is of the opinion that this technical correction strikes a balance between the rights of the spouse and the negative consequences to qualified plans of burdensome recordkeeping requirements. After all, if businesses decide to terminate plans rather than to suffer continual increases in recordkeeping and administrative requirements, the spouses will not be benefitted from these consent provisions at all.

- 6 -

3. Possible Conflict with State Law

It should be noted that SBCA is aware of potential conflict between REA and state law concerning criteria for "informed consent." Various States provide different rules as to what constitutes informed consent, which may be inconsistent with informed consent as finally determined under REA. SBCA recommends that this conflict be eliminated by amending the Act to specifically state that for purposes of the Code and ERISA, the informed consent state law requirements are preempted by provisions in the Code and ERISA, and any regulations or rulings pertaining thereto.

4. Right of Spouse to Consent At Any Time

SBCA also believes that clarification is needed as to when spousal consent may be given to an employee's waiver of survivor benefits. Code Section 417(a)(2) is silent on the matter. The Senate Finance Committee Report states that "this consent is to be given in writing at the time of the participant's election . . .". However, Code Section 417(e)(2) provides that the surviving spouse may consent to immediate distribution of the present value of a survivor annuity. Apparently, Code Section 417(e)(2) would permit a post-death spousal consent, contrary to the Senate Finance Committee Report language. Congress should take advantage of the Act to clarify exactly when the spouse's consent may be given; at the same time it could coordinate the Senate Finance Committee Report language and the statutory language of Code Section

- 7 -

417(e)(2). To this end, SBCA believes that there is no compelling reason why the spouse's consent should be limited to the time of the employee's election to waive the survivor annuity. For example, if the spouse is amply provided for by other means, by a designation to the spouse outright, or by a carefully designed trust for her benefit and the benefit of other members of her family, the spouse should be able to consent to such designation of beneficiary at any time, even after the participant's death. For these reasons, there should be no time limit on the spousal consent.

5. Clarify That Spousal Consent is Not the Transfer of a Property Interest

A related issue is whether the spouse's consent constitutes a transfer of property for gift and estate tax purposes. It appears to SBCA that REA has created a new property right in the spouse. The Code, however, is silent on this issue. Note that Act Section 2(f) provides that if a spousal waiver (to waive a qualified preretirement survivor annuity payable under the transitional rules) is made on or before the end of the plan year to which REA applies, then the spousal waiver is not to be treated as a transfer of property for purposes of federal gift taxes. That provision seems to confirm SBCA's belief that the spousal actions to waive benefits are not to be considered a transfer of property for gift tax purposes. But since Act Section 2(f) addresses only the transitional rules under REA, there remains open the

- 8 -

question of whether an exemption from the gift tax rules applies to other spousal consents under REA. SBCA urges Congress to specifically state in this Act that a spousal consent does not result in the transfer of a property interest.

6. Conflict with Prenuptial Contracts

REA creates possible conflicts between federal law and prenuptial agreements, and such possible conflicts should be avoided by clarifying amendments in the Act. SBCA believes that it is inappropriate for federal law to preempt prenuptial agreements which are valid under state law. Therefore, SBCA urges Congress to specifically state in the Code and ERISA that where a binding prenuptial agreement exists between spouses which addresses the issue of beneficiary designations of pension entitlements, an employee may waive one or both survivor annuities consistent with that binding prenuptial agreement, without an accompanying spousal consent. To this end, Congress should also address the issue of whether a valid prenuptial agreement would, itself, constitute a valid waiver of the survivor annuities (and consent thereto), since the participant and his or her spouse would by definition not be married at the time of the agreement. Furthermore, the same priority should be given to any binding agreement between a plan participant and his spouse entered into during the pendency of an action for legal separation or divorce; otherwise, if such an agreement is entered into and the

- 9 -

participant dies before the divorce is granted, there will be a conflict between the binding contract under state law and the provisions of Federal law.

B. Qualified Preretirement Survivor Annuity Clarification.

Act Section 2(b)(1) generally provides that where an employee separates from service prior to death, qualified preretirement survivor annuities ("QPSA") will take into account only service actually performed until the employee separated from service. Act Section 2(b)(1) is intended to clarify and limit the measure of benefits due to surviving spouses upon the death of the employee prior to receipt of plan entitlements.

SBCA applauds this clarification as a means of eliminating unearned benefits to participants and their spouses, as well as reducing the costs of funding survivor benefits under a qualified plan.

However, since qualified plans were required to provide a QPSA from the enactment date of REA, there exists the possibility that QPSAs were or may be paid in an amount in excess of the amount required, taking into account the clarification made by the Act. SBCA therefore urges that guidance be provided in the Act or elsewhere indicating the manner of recouping benefits paid in excess of that required from a QPSA, as amended by the Act. In this regard, SBCA also

- 10 -

urges that guidance be provided as to how QPSAs should be determined during the period during which passage of the Act is pending.

C. Clarification of Notification For Employees Hired After Age 35

Act Section 2(b)(5) provides that employees who are older than age 35 when hired are to be provided their written explanation of QPSAs within a reasonable period after being hired.

SBCA recommends that the explanation be provided upon the employee's becoming vested in any portion of his entitlements derived from employer contributions under the plan. This would be consistent with Joint Committee of Taxation's recommendations and would better coordinate selection of the form of preretirement benefits with their availability to the employee under the plan. Joint Committee on Taxation, Description of H.R. 2110 Relating to Technical Changes to the Retirement Equity Act of 1984 (JCS-14-85), May 14, 1985, Section B.5. It would also make more relevant the receipt of the explanation by the employee. Receipt of the explanation prior to the employee's eligibility to receive a QPSA would likely not be given the requisite attention by the employee. Delay in receipt of the explanation until after the participant is vested in any portion of his plan entitlements (as may occur if the explanation is provided three years after

- 11 -

the date of hire, as proposed by the Joint Tax Committee) may preclude a participant's opportunity to waive the QPSA when he is entitled to do so by law. *Id.*

In this regard, SBCA also recommends that Code Section 417 be amended to permit vested employees who have not yet attained age 35 to receive their explanation of QPSAs at the time they vest in any portion of their plan benefits, and permit them to waive that form of benefit if they so desire (with their spouse's consent) at that time. Not only would this eliminate an arbitrary distinction between who must receive a QPSA and who may receive a QPSA, but it would also permit plan administrators to develop a uniform procedure for distributing QPSA explanations to plan participants. This would be especially beneficial to small businesses who administer their own plans. Moreover, this amendment would obviate potential 5th Amendment due process issues arising as a result of the impairment of an age group's right to contract and, where contractual rights already exist, from the deprivation of property without due process of law.

D. Clarification of Impact of Fully Funded
Survivor Annuities on Waiver, Consent and
Notice Requirements under Code Section 417.

SBCA believes that it would be appropriate to amend the Act to specifically state that where a plan fully subsidizes one or both of the survivor annuities, only the notice requirements pertaining to the fully subsidized annuity(ies) are exempted. REA as currently enacted states that Code

- 12 -

Section 417(a) shall not apply to fully subsidized survivor annuities. Code Section 417(c)(4). This may be interpreted to mean that where the survivor annuities are fully funded the survivor annuity form of benefit may not be waived (nor consented to by the spouse), resulting in the mandatory provision of survivor annuities to married participants, in accordance with Code Section 401(a)(11)(A).

Clearly this was not the intent of Congress. The Senate Finance Committee Report pertaining to Act Sections 103 and 203 states that "a plan is not required to provide notice of the right to waive the [survivor annuities] if the plan fully subsidizes the costs of the benefit." (Emphasis added). Consequently, the Code and ERISA should be amended by way of the Act to reflect this intention. Not only would this conform the law to Congressional intent, it would eliminate a potential restriction on the forms of benefits that may be paid, despite the preference of the participant and his or her spouse to the contrary.

E. Clarification of Exclusion of Voluntary Contributions

Since the Act seeks to amend Code Section 401(a)(11), SBCA believes that this would be an appropriate time to clarify that Section to provide that the survivor annuity rules apply only to employer and mandatory employee contributions. Nondeductible after-tax employee contributions are generally

- 13 -

considered a savings mechanism and therefore not part of a true retirement program. Therefore, SBCA believes that requiring survivor annuity provisions to apply to voluntary after-tax employee contributions would be inappropriate and that the Code and ERISA should be amended to so state.

III. Spousal Consent Requirements - Expansion to Plan Loans

A. Practical Effects of Act Section 2(b)(4) - Recommendation

Act Section 2(b)(4) provides that no portion of a participant's accrued benefit may be used as security for a loan unless the participant's spouse (if any) consents in writing to such use. The Act mandates that the above requirement be incorporated in the plan document. These provisions apply to loans made after April 18, 1985, or revised, renewed, extended, or renegotiated after that date.

SBCA recognizes that the amendment is consistent with the concept of protecting spousal rights under qualified plans. Thus, it necessarily would follow that loans secured by the vested benefit should themselves provide for a spousal consent.

Nevertheless, SBCA recommends the deletion of Act Section 2(b)(4) for the following reasons: (1) the requirement will add yet another layer of complexity and paperwork upon the administration of qualified plans; (2) the costs of operating the plan will again increase; (3) legal fees will increase to

- 14 -

protect or defend the plan and its trustees against suits by spouses who, due to a lack of guidance in the Code and Regulations or from the Internal Revenue Service, may not have been provided sufficient information to give "informed" consent as to this use of Plan assets; (4) increased legal costs will arise if the plan has already been amended for REA and must be re-amended to provide for this consent requirement; and (5) employer-employee relations may deteriorate if the additional restriction on plan assets is perceived as a restriction on plan entitlements by the employees. Taken together, SBCA believes that these reasons outweigh the additional protection afforded to spouses as a result of this provision.

Requiring spousal consent for use of plan assets as loan security will add to the already overwhelming complexity and paperwork of administering qualified plans. This addition will be particularly onerous to small businesses, since they are less likely to have the financial resources, personnel or expertise to adequately handle the increased operational functions of qualified plans. While small businesses recognize the need to protect spousal rights under qualified plans, SBCA has already perceived increasing levels of frustration from small businesses as a result of the existing high level of complexity. Where small business owners once established qualified plans to provide their employees with additional benefits, there is an increasing sentiment that qualified plans are more trouble than they are worth. This sentiment can only

- 15 -

be enhanced by a provision which requires additional administration and paperwork. It is one thing to provide rules that effectively ensure that participants and beneficiaries receive their retirement benefits. It is another matter entirely when, as a result of legislation requiring amendment upon amendment, businesses become so overburdened and disenchanted that they terminate their qualified plans, thereby eliminating retirement benefits completely.

The spousal consent for loans involving plan assets will also increase the costs of administering the plan. New consent forms and procedures will have to be created. This will require additional professional fees to be paid in order to provide guidance as to the necessary informed consent (to the extent this can be determined without guidance from the Code, Regulations, or the Internal Revenue Service). In addition, valuable personnel resources will have to be used to administer this use of plan assets and the obtaining of required consents. If the small business utilizes an outside administrator for the plan, the increased administration to provide the spousal consent will be reflected in higher administrative fees.

Small businesses will have to establish procedures to obtain the spousal consent, which should also involve explaining the consequence of a plan loan to the employee and his or her spouse. Besides taking up valuable time, it is doubtful that small businesses (or personnel assigned to the

- 16 -

task) will be sophisticated enough to determine whether the spouse was properly informed, or whether the consent will be valid under law. This problem is exacerbated by the lack of guidance regarding spousal notices and informed consent under REA. As a result there will be increased exposure to litigation involving the qualified plan, its trustees and/or administrators, as well as exposure by plan advisers (such as attorneys, accountants, and administrators) to malpractice lawsuits. (Discussion of the necessity to clarify what is "informed consent" may be found at Section 11.A, *infra*). This will increase legal fees to the small business in two ways. First, legal advice will be necessary to provide safeguards (to the extent possible) against such litigation. Second, should a lawsuit arise due to the spousal consent requirements, legal costs will be incurred to defend the action.

The Act also requires that the plan document provide for the spousal consent to participant plan loans. To the extent the plan must be amended to provide for this requirement, the cost of amending and restating the plan will increase.

SBCA also anticipates a decrease in employee morale as a result of this amendment. Small businesses maintaining plans which provide for the use of plan assets as security for loans generally emphasize this availability as a means of enhancing employer-employee relations. Requiring spousal consent may be viewed by employees, at a minimum, to be an impediment to a

- 17 -

participant's access to this plan benefit. This may result in the perception by employees that the qualified plan is not the employee benefit it was represented to be, thereby damaging the employer-employee relationship.

As a result of increased costs, risks, and complexities attributable to requiring spousal consent for the use of plan assets, SECA fears that small businesses will terminate the relevant provisions from their plans, or worse, terminate their plans in entirety. We recognize the desire by Congress to minimize threats to the spouse's receipt of his or her plan entitlements. However, SECA believes that the negative consequences of Act Section 2(b)(4) to small businesses outweigh the increased protection of spousal benefits under qualified plans.

SECA has also noted a problem relating to the effective date of Act Section 2(b)(4). It is likely that subsequent to April 18, 1985, some plans have permitted use of plan assets as loan security without the required spousal consent. This may have occurred due to a lack of publicity regarding the Act, especially to the general public. Moreover, there will be uncertainty as to all plan loans until the Act is enacted. Therefore SECA urges that if Act Section 2(b)(4) is not deleted, it be amended to apply on or after date of enactment, and not before.

- 18 -

B. Suggested Clarifying Amendments

Should Congress determine that Act Section 2(b)(4) be retained, SBCA suggests that the following clarifying changes be effectuated:

1. Have Act Section 2(b)(4) made effective as of date of enactment. (See discussion above)
2. Permit Act Section 2(b)(4) to be applied without requiring incorporation into the plan document.
3. Provide a "safe harbor" as to what would constitute informed consent to the spouse. (See discussion at II.A. infra.)

C. Remaining Technical Issues

In addition, we have noted the following technical issues that we believe should be resolved if Act Section 2(b)(4) is to be retained.

1. Determine whether increased plan expenses attributable to providing these spousal consents for the use of plan entitlement as security for a loan may be taken into account in an equitable manner by the plan, similar to expenses attributable to the provision of survivor annuities. (See Code Section 417(f)(4)).

- 19 -

2. Clarify what type of consent is necessary. SBCA suggests either cross referencing to Code Section 417(a)(2) (but taking into account the change to that Section proposed by the Act (See II A., *infra*)), or providing a separate Code Section addressing the proper manner of spousal consent for loans.

IV Transferee Plan Rules

Act Section 2(b)(2) amends Code Section 401(a)(11)(B)(iii) to provide that a defined contribution plan other than a money purchase pension plan is not a transferee plan (for purposes of determining whether a plan must provide survivor annuities and comply with Code Section 417) with respect to a participant if a transfer from a plan required to provide the survivor annuities occurs before January 1, 1985. SBCA believes that small businesses would more easily be able to administer their plans, and determine whether survivor annuities will have to be paid, if Act Section 2(b)(2) were amended to provide that a plan described under Code Section 401(a)(11)(B)(iii) is a transferee plan only with respect to transfers made on or after plan years beginning after January 1, 1985.

The reason for this amendment is that January 1, 1985, is an arbitrary date to any plan which is not operated on a calendar year basis. Since REA generally requires that the survivor annuity provisions apply as of the first plan year beginning on or after January 1, 1985, SBCA believes it is

- 20 -

inconsistent to require that survivor annuities be provided on account of an event which occurred prior to this effective date. Moreover, this amendment would avoid legal and actuarial costs necessary to amend this plan to provide these survivor annuities where, except for this transfer, it is the intent of the employer not to provide this form of benefit.

Act Section 2(b)(2) also provides that a separate account must be maintained for transferred assets. The Joint Committee on Taxation in its explanation of this provision also states that if separate accounts for transferred assets are not maintained, then the survivor benefit requirements will apply to all benefits payable with respect to the employee under the plan.

SBCA understands that the purpose of this provision is to prevent having to pay a survivor annuity on transferred amounts even though such form of benefit as required for the other benefits under the transferee plan. However, the Joint Committee on Taxation language regarding the maintenance of separate accounts is very broad in its scope, conceivably requiring separate accounts to be maintained where both the transferred assets and the transferee plan do not require that survivor annuities be paid. Therefore, in order to minimize additional recordkeeping to the extent possible, SBCA recommends that guidance be provided specifically addressing

- 21 -

where separate accounts do have to be maintained and where separate accounts are not required.

V. SEP Eligibility

Act Section 2(a)(4) amends the eligibility requirements of Simplified Employee Pensions (SEPs), in pertinent part, from attainment of age 25 to attainment of age 21. SBCA is in favor of consistent eligibility requirements for SEPs and qualified plans. In this regard, however, SBCA is concerned that delay in enactment of the Act may cause uncertainty as to whether employees from age 21 to age 24 should be covered in the SEP by the employer. This may cause employers to have to choose between covering more employees than it needs or wants to, or risking disqualification of the SEP for failure to cover the necessary employees under law.

SBCA believes this potential conflict could be avoided by enactment of this Act as soon as possible. This will provide the necessary certainty required for complying with SEP eligibility requirements. Moreover it will allow employers the time to fund the SEP to take into account all eligible employees. Alternatively, in the event that this Act cannot be enacted until a later date, SBCA recommends an amended effective date for SEP eligibility which reflects the delay. This will minimize eligibility coverage and funding problems that could conceivably apply to employers sponsoring SEPs.

- 22 -

VI. Lump Sum Treatment; Recapture of Taxes

Act Section 2(a)(2) provides that for lump sum purposes, determination of the balance to the credit of an employee shall not take into account an increase in vesting which could occur upon reemployment. However, that Section also provides that if lump sum treatment were elected by the employee, and the employee was reemployed by the employer, any increase in the vested portion of the employee's pre-break accrued benefit will cause a recapture of taxes which were avoided by use of favorable taxation methods available on lump sum distributions.

SBCA objects to the recapture of previously taxed distributions under the Act as currently proposed. This recapture amounts to a tax upon rehiring an employee, creating a significant disincentive for an employee to return to a former employer. As a result, it will be more difficult for a small business to rehire a former employee within the break in service period as amended by REA. Given the extreme demand for talented employees, any provisions in any law which discourages the employee from being able to freely consider all possible opportunities for advancement, including reemployment by a former employer, should not be enacted or should be eliminated. SBCA believes that the recapture tax is just such a provision and as such should not be enacted.

Assuming, arguendo, that the recapture tax is retained, SBCA urges that it be specifically made clear that any tax paid

- 23 -

under Code Section 402(e) (the ten year forward averaging provisions) or the recapture tax, be applied to reduce taxes payable on the subsequent distribution from the retirement plan. In effect, a permanent "lookback rule" should be provided. To do anything less is to provide a double tax on the distribution of plan entitlements. Moreover, it is urged that a method be devised to index the tax paid to take into account the present value of paying taxes immediately rather than upon the ultimate distribution of plan entitlements.

SBCA also wishes to note that Code Section 402(f) appears to require that upon certain distributions of benefits, employees should receive notice as to the provisions of Act Section 2(a)(2). We urge that immediate guidance be provided by the Internal Revenue Service as to what constitutes proper notice of these provisions. For example, it should be determined whether mere notice of the existence of the recapture tax (and/or its illustration) is sufficient, or whether a computation of the actual potential recapture with respect to the employee in question is required.

To this end, SBCA recommends that Congress mandate the Treasury to provide by regulation a "safe harbor" of information which, if included in a notice, would satisfy Code Section 402(f). Furthermore, we remind the Committee that the Internal Revenue Service is required to furnish an officially approved notice which administrators may use to explain

- 24 -

available rollover treatment or, if applicable, 10-year averaging and capital gains treatment. Senate Finance Committee Report on the Retirement Equity Act of 1984, Section 207. It is urged that this notice also provide officially approved language which addresses Act Section 2(a)(2).

3321T

FRANK J. SNELL
EDWARD JACOBSON
JOHN J. BOUMA
H. WILLIAM FOR
LOREN W. COUNCE JR
WARREN E. PLATT
WILLIAM A. HICKS
DANIEL J. MAULIFFE
DONALD D. COLBURN
DOUGLAS W. SETZ
JOSEPH T. MELTZER
CHARLES H. AYERS
MICHAEL S. MILRO
BARRY D. HALPERN
JOEL R. MORSE
LONNIE J. WILLIAMS JR
VAUGHN A. CRAWFORD
THOMAS J. KENNEDY
WILLIAM D. FEARROW
JOHN BERRY
SMURLEY J. WALK
ISABELLE T. MORRIS
JUDY M. MILLER
PRESTON H. LONGINO JR
STEPHEN C. NERMARK
DOUGLAS J. GILBERT
MATTHEW W. KEENEY
LOIS R. SAVAGE
BRUCE P. WHITE
MICHAEL J. CANCE JR
PATRICK E. HODG
DAVID A. DAMORE
MICHAEL L. BHEES
JODY K. FALK
TERESA DAVIDSON

FOR COUNSEL
FROM LEAVE OF ABSENCE

MARY WILMER
MAYNARD R. GOUDY
JOHN P. HALLIPS
RICHARD MULLER
JOHN S. COHEN
GUY D. GELBRON
GEORGE H. LYONS
BRUCE D. PROGRIE
MICHAEL D. TERRY
GREGOR H. EISEN
WILLIAM R. HAYDEN
ROBERT B. HOFFMAN
LAWRENCE F. WINTHROP
CHARLES A. B. SCHOFF
CHARLES H. TRAEGER
RICHARD W. SHEFFEL
MICHAEL P. ANTHONY
SUZANNE HEGAN
ARTHUR T. ANDERSON
JOYCE ALAN WRIGHT
DAVID A. SPRENTALL
KATHERINE H. ANKENY
KIMBERLY J. GRABER
MARGARET J. STENER
DORA THOMAS
T. BORNARD JR
REBECCA WINTERSCHIEDT
VICTOR SOTOMAYOR
JOSEPH A. REINHARDER
GEORGE J. COLEMAN
JEFFREY B. MESSING
BRYANT D. BARBER
CRAIG K. WILLIAMS
JAMES J. OSBORNE
SCOTT A. HOLCOMB

JOSEPH T. MELTZER JR
FREDERICA R. STENER JR
ARTHUR C. DEER
ROBERT C. BATES
THOMAS J. BELL
JAY D. WILEY
PETER J. BATHWELL
STEVEN M. WHEELER
MARY J. LEADER
ROBERT J. DEERY
JAMES W. REYNOLDS
GERARD MORALES
ROBERT J. GIBSON
THERESA A. GABALDON**
JAMES R. CONDO
MARCIA J. BUSCHING
RICHARD C. UNDERWOOD
BRENT D. ELLSWORTH
PETER G. BANTIN
JOSEPH A. DUNN
JANNA P. BRADY
JAMES P. MUEHLBERGER
ROBERT H. OBERBILG
H. MARC JOSEPH
WILLIAM A. CLARKE
JAMES D. MILLER
JAMES J. SIENCK
JAMES D. EHINGER
EILEEN J. MOORE
MARLAN C. WALKER
GORDON H. MASSON
YVETTE E. COHEN
DOUGLAS H. ALTSCHULER
JEREMY D. HUSSEMAN
CHERYL A. KEGAN

LAW OFFICES SNELL & WILMER

300 VALLEY BANA CENTER
PHOENIX ARIZONA 85073
(602) 257-7211

TELEX 65088
TELECOPIERS
MANUAL (602) 257-7211
AUTOMATIC (602) 256-2735

May 30, 1985

Honorable Dan Rostenkowski
Honorable John J. Duncan
Honorable William L. Clay
Honorable Marge Roukema
United States House of Representatives
Washington, D.C. 20515

Dear Congressmen Rostenkowski, Duncan and Clay and
Congresswoman Roukema:

We understand that you recently introduced HR 2110, the proposed Technical Corrections Act to the Retirement Equity Act of 1984 ("REA"). After working with the REA for the past several months, we respectfully suggest that you consider expanding HR 2110 in order to clarify the scope of the special rules for "fully subsidized" plans prescribed by Section 417(a)(4)(A) of the Internal Revenue Code (the "Code") and Section 205 (c)(4)(A) of the Employee Retirement Income Security Act of 1974 ("ERISA").

As will be fully explained below, Section 417(a)(4)(A) of the Code and Section 205(c)(4)(A) of ERISA should be amended to clearly state whether a participant in a "fully subsidized" plan may waive the qualified preretirement survivor annuity prior to age 35. In addition, Section 417(a)(4)(B) of the Code and Section 205(c)(4)(B) of ERISA should be modified to clarify the circumstances under which a plan will be deemed to be "fully subsidized".

We will keep our comments as short as possible, but we are willing, of course, to expand on the points raised below and welcome questions from you or members of your staff.

Waivers Prior to Age 35.

Section 417(a)(4)(A) of the Code and Section 205(c)(4)(A) of ERISA read as follows:

The requirements of this subsection shall not apply with respect to the qualified joint and survivor annuity form of benefit or the qualified preretirement survivor annuity form of benefit, as the case may be, if the plan fully subsidizes the costs of such benefit.

Read literally, the above quoted language relieves a fully subsidized plan from compliance with all of the requirements of Section 417(a) of the Code and Section 205(c) of ERISA. The notice provisions found in Code Section 417(a)(3) and ERISA Section 205(c)(3) appear to be inapplicable to fully subsidized plans. More importantly, Code Section 417(a)(4)(A) and ERISA Section 205(c)(4)(A) seem to indicate that a fully subsidized plan need not observe the requirements of Code Section 417(a)(5) and ERISA Section 205(c)(6), which preclude participant waivers of the qualified preretirement survivor annuity prior to the attainment of age 35. As a result, a participant in a fully subsidized plan should be allowed to waive the qualified preretirement survivor annuity at any time, regardless of his or her age.

Despite the clear language of Code Section 417(a)(4)(A), the Internal Revenue Service has adopted an unnecessarily narrow interpretation of its provisions in its recently published "Defined Contribution Listing of Required Modifications and Information Package" (the "LRM"). Although the LRM allows a fully subsidized plan to avoid compliance with the notice requirements of Code Section 417(a)(3), fully subsidized plans are required to preclude participant waivers of the qualified preretirement survivor annuity prior to age 35.

The sole support for the narrow reading advocated by the IRS is a single sentence in the Senate Finance Committee Report to the REA, which states that "[u]nder the bill, a plan is not required to provide notice of the right to waive the qualified joint and survivor annuity or the qualified preretirement survivor annuity if the plan fully subsidizes the cost of the benefit." In order to resolve the

inconsistency between the above-quoted passage in the Senate Finance Committee Report on which the IRS apparently relies and the clear language of the statute, we suggest that HR 2110 modify Code Section 417(a)(4)(A) and ERISA Section 205(c)(4)(A).

Section 417(a)(4)(A) of the Code and Section 205(c)(4)(A) of ERISA should be amended to specifically provide that a fully subsidized plan need not comply with the notice requirements of Code Section 417(a)(3) and ERISA Section 205(c)(3). The revised sections should also indicate that the election period provisions of Code Section 417(a)(5) and ERISA Section 205(c)(6) are either inapplicable or that a participant may waive the qualified preretirement survivor annuity provided by a fully subsidized plan at any time. In order to alleviate any confusion, revised Code Section 417(a)(4)(A) and revised ERISA Section 205(c)(4)(A) also should state that a fully subsidized plan must comply with the participant waiver and spousal consent provisions included in Code Section 417(a)(1) and (2) and ERISA Section 205(c)(1) and (2).

Meaning of "Fully Subsidized".

Section 417(a)(4)(B) of the Code and Section 205(c)(4)(B) of ERISA state that "a plan fully subsidizes the costs of a benefit if under the plan the failure to waive such benefit by a participant would not result in a decrease in any plan benefits with respect to such participant and would not result in increased contributions from such participant."

With the advent of the REA, many plan sponsors have decided to comply with the qualified preretirement survivor annuity requirements by redesigning the death benefit provisions of their plans. Participants are not required to increase their contributions in order for their spouse to receive the survivor annuity and no benefits are lost as the result of the participant's failure to waive the survivor annuity. The death benefit provided by the plan is simply redirected from the participant's designated beneficiary (who may or may not have been the participant's spouse) to the spouse.

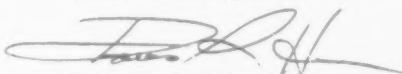
In our view, a plan does "fully subsidize" the qualified preretirement survivor annuity if it applies the pre-REA death benefit to payment of the survivor annuity,

since no plan benefits are in fact reduced. The sum total of benefits payable as a result of the participant's death will be the same both before and after the amendment to comply with the REA. The amendment simply changes the recipient of these benefits.

Recent comments made by representatives of the Internal Revenue Service call our interpretation of the "fully subsidized" definition found in Section 417(a)(4)(B) into question. In order to clarify matters, we suggest that you modify Code Section 417(a)(4)(B) and its ERISA counterpart, Section 205(c)(4)(B), to provide that a plan fully subsidizes the cost of a benefit if under the plan the failure to waive the benefit does not result in either (1) increased contributions from the participant or (2) a decrease in any plan benefit other than a death benefit. The revised sections could also indicate that the reduction of a death benefit would be permitted without jeopardizing a plan's fully subsidized status only if the sum of the present actuarial value of the qualified preretirement survivor annuity plus any remaining death benefits is at least equal to the value of the pre-REA death benefits provided by the plan.

Thank you for your consideration of our comments.

Very truly yours,



Thomas R. Hoecker
For SNELL & WILMER

TRH:bav

05TRH0701

LAW FIRM
 WILLIAMS & CONNOLLY
 HILL BUILDING

EDWARD BENNETT WILLIAMS
 JAMES W. CONNOLLY, M.F.A. 1978
 ROBERT A. SCHULMAN
 VINCENT J. FULLER
 RAYMOND W. BERGAN
 WILLIAM E. BEDEL
 JEROME J. COLLINS
 ROBERT J. WEINBERG
 DAVID PUGH
 STEVEN M. JAMES
 JOHN W. LARDMAN, JR.
 PAUL MARTIN HOLLY
 J. R. ALCAZARATH
 CHARLES W. WATSON
 JOHN S. KESTER
 WILLIAM E. HODANELL
 BRENDAN J. SULLIVAN, JR.
 A. BREWSTER DAVIS, III
 RICHARD M. GORDON
 ROBERT P. WATKINS

JERRY L. SHULMAN
 LAWRENCE J. JOHNSON
 JEROME J. FERGUSON, III
 ROBERT B. BARNETT
 DAVID E. KENDALL
 JOHN J. BUCKLEY, JR.
 JEROME J. SCHWARTZ
 JOHN G. ALAN MARLIN
 JOHN W. VICK
 BARRY S. KATZ
 KEVIN T. BARR
 STEPHEN J. LUBANOWSKI
 PAUL W. WARD
 R. J. DECK, M.F.A. 1978
 FREDERICK W. HATTEN PETERSON
 PETER J. KATZ
 JUDITH A. MILLER
 DON R. BARR
 ALICE M. KANE MARSH
 MICHAEL S. SUNDENMEYER

400 PENNSYLVANIA STREET, N.W.
 WASHINGTON, D.C. 20006

AREA: 202-331-1000
 TOLL FREE

JAMES J. TULLER, JR.
 STANLEY J. JACOBSON
 DAVID W. JACOBSON
 BRUCE W. JACOBSON
 CAROLYN D. WILLIAMS
 F. LEO HERRICK, III
 STEVEN M. HARRIS
 JEROME A. FINE, JR.
 KAREN S. JOHNSON
 ROBERT S. LEE
 ROBERT W. BENTLEY, JR.
 PAUL W. LEE
 JOHN E. KAHN, JR.
 JEFFREY F. FOLEY
 HENRY M. LEE
 HENRY J. LEE, JR.
 J. CLAYTON LAMSON
 RICHARD S. HOFFMAN
 STEVEN A. STEINBERG

W. HOWELL P. JONES
 STEVEN A. BERRY
 STEVEN J. COOPER
 ROY J. WAT
 WARD J. J. JONES
 JOHN A. STALL
 WARD E. FERGUSON
 STEVEN S. JOHNSON
 JAMES S. McLEOD
 JEFFREY A. HALL
 DAVID L. HALL, JR.
 GEORGE E. WOOD
 JAMES P. KATE
 JEFFREY M. TAYLOR
 JAMES H. HARRIS
 WARD E. J. ROBERTS
 J. W. H. CONNOR, JR.
 JAMES H. HARRIS
 ROBERT W. HARRISON

CLAY
 WARD E. J. ROBERTS
 JAMES H. HARRIS
 J. W. H. CONNOR, JR.
 JAMES H. HARRIS
 ROBERT W. HARRISON

June 7, 1985

BY HAND

The Honorable William L. Clay
 Chairman
 Labor-Management Relations Subcommittee
 2451 Rayburn House Office Building
 Washington, D. C. 20515

Re: Technical Corrections to Retirement Equity Act of 1984

Dear Congressman Clay:

This comment is submitted to outline a transition rule problem caused by the Retirement Equity Act of 1984 ("REA"), that we ask be addressed in the Subcommittee's consideration of technical corrections to REA embodied in H.R. 2110.

Briefly, the facts are as follows: We represent the daughter of a gentleman who died prior to retirement in early September, 1984, only a few days after enactment of the Retirement Equity Act. Under his estate plan and will, which had been carefully planned over the years, the major portion of his estate went to the benefit of his wife, leaving her very wealthy. His will had been changed after ERTA, to remove his daughter as an immediate beneficiary in favor of the wife, to take advantage of the unlimited marital deduction. To provide for his daughter financially, he changed the beneficiary designation forms with his retirement plans to make her the beneficiary, rather than his wife.

The deceased gentleman died with no knowledge whatsoever of the Retirement Equity Act or the requirements of a waiver. As a result of the Act, in particular the transition rule provisions

of Section 303, the retirement plans are refusing to pay the survivor benefits to the daughter unless the mother executes waivers. The mother, however, is unwilling to waive those benefits. The plans view the Act as requiring the survivor spouse be provided with survivor death benefits in the form of a preretirement survivor annuity, even though the participant had no knowledge of the Act or opportunity to obtain a waiver.

The result here is completely contrary to the intentions of the deceased. We submit that the result is also contrary to the underlying purpose of the Retirement Equity Act, since the surviving spouse was more than adequately provided for. We also question whether Congress intended, in its immediate effective date provision embodied in Section 303, to overturn legislatively the intentions of a decedent under these facts.

We urge that consideration be given to a legislative correction to this problem in connection with H.R. 2110, the technical corrections bill concerning REA. A very narrow transition rule could be drafted, applicable only to a participant who died having no notice of REA, and who had adequately provided for his spouse financially as measured by some objective standard.

One approach might be for the exception to apply only if all the following conditions applied:

1. Participant Died in Transition Period: The plan participant died after the enactment date, but prior to the general effective date of REA (plan years beginning after December 31, 1984), and left an otherwise valid designation of someone other than his or her spouse as the beneficiary of the preretirement survivor benefits;
2. Participant Died Without Notice: The plan had not, prior to the beneficiary's death, provided notice to the participant of the requirements of REA regarding spousal waivers and the participant did not know, and could not reasonably be deemed to have known, of such requirements; and
3. Spouse Adequately Provided for by Non-Plan Assets, As Measured Objectively: The participant adequately provided for his or her spouse financially, under the

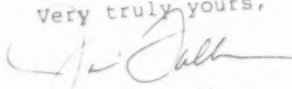
will or otherwise, as measured by an objective standard such as:

- a. The present value of income to the surviving spouse from his or her inheritance under the deceased spouse's estate exceeds the present value of the survivor benefits designated for the non-spouse beneficiary, or exceeds it by some multiple; or
- b. The present value of income to the surviving spouse from his or her inheritance from the deceased spouse exceeds some specified amount; or
- c. A combination of (a) and (b), or (a) and (b) as alternatives.

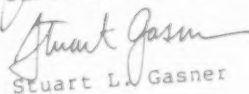
We greatly appreciate your consideration of this problem. We request the Committee to include a statutory provision covering this problem in H.R. 2110 when reported out of Committee. If it would be helpful, we would be pleased to submit more information or meet with you or your staff to discuss the issue in more detail.

Thank you very much for your attention to this matter.

Very truly yours,



James T. Fuller



Stuart L. Gasner

SLG:tk